DON'T MAKE A PROFIT, CREATE A FORTUNE

Build the Business of Real Estate Wealth Creation

Bill Syrios, Andrew Syrios, Amanda Perkins & Ryan Dossey

DON'T MAKE A PROFIT,
CREATE A FORTUNE

Ryan, Amanda, Bill & Andrew

TheGoodStewards.com

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This book is a work in progress.
What follows includes many links accessible for further study.

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STEWARDSHIP PROPERTIES

Why the name Stewardship?

Although it was not as clear back in 1989, when our business consisted of one property, the hope was to build a company that would be about more than just making money.

Profit is to a business what air and water are to life. We must have them, or we die. Likewise, without profits, a company will fail. However, we don't live for the air we breathe or the water we drink. They are a means to higher end. Our greater purpose for wealth-building is *the increased and unexpected opportunities that come with creating wealth for our entire team—staff, partners, contractors, vendors, lenders, investors—to serve our residents in their housing needs.*

The name *stewardship* comes from the perspective that we are all "just passing through this life." While here, it is most appropriate to consider ourselves not as owners of things or as expert opportunists, but as managers, or better yet, stewards in the service of others.

The Psalmist writes, *The Lord owns cattle on a thousand hills.* This sentiment leaves no doubt as to who owns all the real estate under the cows' feet as well! Another verse reminds us of what's at stake: *Unless the Lord builds the house those who build it labor in vain.*

Good stewards take on the task of skillfully managing that which they have been entrusted with for the benefit of all those involved. Applied to real estate—that's who we are and what we do.

It is required of stewards that they be found trustworthy.
-The Apostle Paul, 1 Corinthians 4:2

INTRODUCTION to
Bill, Andrew, Amanda & Ryan

SO, YOU WANT TO CREATE A FORTUNE?

There are a relatively limited number of ways for a person to become wealthy. Granted this list of ten isn't exhaustive, but it covers many:

1) Win the lottery
2) Marry a wealthy person
3) Come into an inheritance
4) Become a best-selling author
5) Invent something innovative (or the pet rock)
6) Have "mad skills" as a professional entertainer or athlete
7) Become a famous and highly sought-after actor or actress
8) Be a great stock picker who knows when to buy and sell
9) Gain specialized knowledge in a field—be handsomely rewarded
10) Build a business that becomes very valuable

BILL'S STORY: From Hobbyist to Business Builder

When I first looked over this list in my mind's eye over 30 years ago, it didn't take long for me to eliminate numbers 1 through 9. That left only one option – number 10.

But not only did I have a narrow path to creating wealth, I also had another set of problems. My dad was an attorney, my mom was a school teacher, and my chosen profession was campus ministry. In college, I studied to become a history major and didn't take a single business class. In seminary, I majored in theology and pastoral studies. No business classes were offered there, not even one on how to more effectively take up the offering! Building a business wasn't in my family DNA, nor had I a day of training in it, nor, frankly, did I have the skillset or any good ideas on how to develop one.

I had heard there was yet another way the average person could become well off: invest in real estate. At first, I thought maybe this 11th option would "cure" my business deficiencies, allowing me to create a pathway to financial success and independence. As I bought my first investment property, my second, then a third and fourth, I labored under this mistaken impression that building a real estate portfolio was something quite different than building some other "normal business."

If you could transport yourself back to the early '80s in Portland, Oregon, you'd see me struggle and bend under the weight of not being business-minded. When it came to operating a coherent investment strategy, overseeing cost-effective rehab, being a common sense landlord, figuring out finances and lending, I was making it up as I went along, and it began to show.

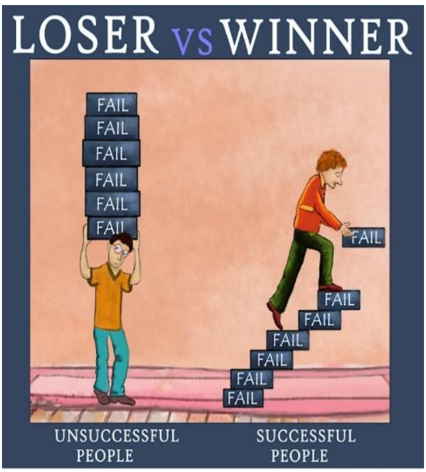
Perhaps I could have survived these shortcomings, but then came a nasty national recession. The housing market imploded (the early '80s version of the late 2000s) and, with it, the timber industry went into freefall. Oregon's economy was then largely based on lumber, so instead of a recession, the state went into a near depression. Interest rates rose nationally to 15% and Oregon real estate prices fell 20-40%.

My job as a campus pastor led me to relocate to Eugene, Oregon and work at the University of Oregon. This move gave me the impetus to unload three of my four Portland properties and "get out of Dodge" with only modest losses. I had to remind myself of a quote often attributed to Winston Churchill:

Success is never final. Failure is never fatal.
It's the courage to continue that counts.

For a time, I went into hiatus from real estate investment to lick my wounds but, try as I might, I could not control my wandering eye. Most every morning I'd find myself perusing the real estate classifieds in our local newspaper (yes, it was pre-internet).

Then in 1989, three years after moving to Eugene, I found myself flat on my back with Hepatitis A and two weeks to look at the ceiling. I loved campus ministry, but I was now 35 years old and could see it coming to an end for me. When it did, what would I do next? I reflected on what I really enjoyed doing and what could be a source of income for my family. I admitted to myself that I was drawn to the thrill of real estate investing. I knew of its wealth-creating potential too, but I also wondered if I could make it a success.



A book I was reading at the time, made all the difference. Achieving the self-imposed (but nevertheless accurate) title of "world's lousiest landlord" had led me to pick up a book on property management for help. The author was taking me to task for my nonchalant, laissez-faire approach and gave me a new paradigm. He said you must treat real estate investment as the business it is… from day one, property one.

Laissez-faire is a French word that means "leave it to itself." This motto works about as well in a business context as it does for child-rearing! Now I was putting two and two together. If real estate is a business, like owning a restaurant, a veterinary clinic or a pot dispensary (hey, it's Oregon), then laissez-faire must be replaced with a focus on developing systems and finding quality people to run them.

Such a mindset was not an issue for my second son (of four), Andrew, who picked up a knack for real estate investing while in college. He and my son, Phillip were business grads from the University of Oregon. Andrew moved from the West Coast to Kansas City, Missouri in January, 2011 to start a real estate investment company from scratch.

***FOR YOUR VIEWING PLEASURE:** If you'd like to watch a video by Bill on this topic, check out: youtube.com/watch?v=-PzYXzUJnqI&t=1870s

ANDREW'S STORY: Gutting It Out Until It Paid Off

Beginnings aren't always easy; starting a business is no exception. But with everything you do, there are always lessons in the setbacks. When I moved to Kansas City in January of 2011, I lived in the basement of the office we bought for the company. On my fourth day there was an ice storm, and the temperature dropped below zero. It felt like a sign that I made a dire mistake. Suffice to say the office basement was a cold, dark and lonely place.

A few months later, we bought a terrible apartment complex and inherited some ill-tempered renters who used drugs; we had to pay them to leave. At the lowest point, my dad and I entertained closing up shop because our cash flow was so poor.

Fortunately, we fought through those challenges. Once we got some of our vacant properties rented, we were able to stabilize and move forward. Now, after that very humble beginning and the innumerable mistakes that came with it, we have gotten pretty far and own nearly 500 houses and apartment units in the Kansas City metro area.

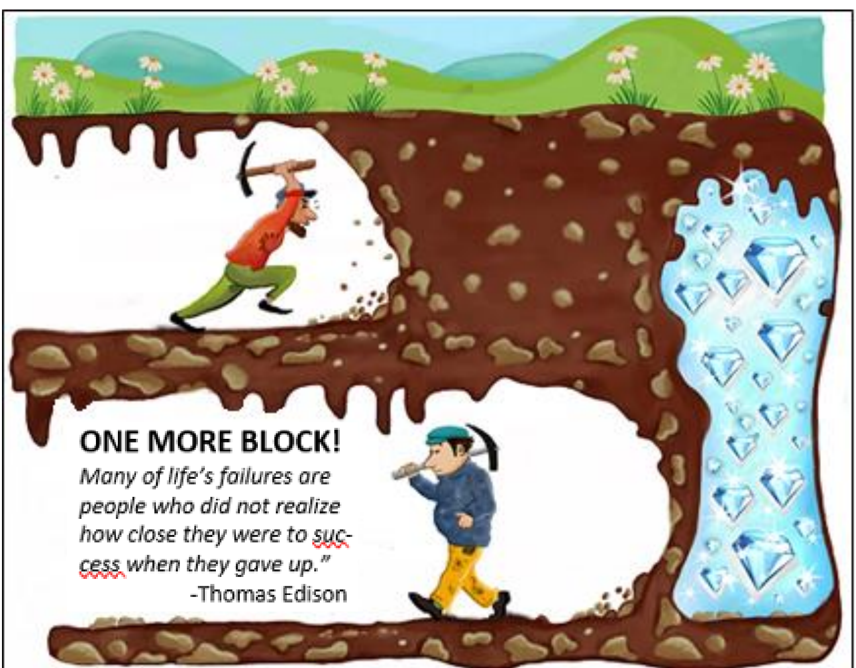
My brother, Phillip, who joined me nine months later in September of 2011, has a sign in his office that reads "make more mistakes." This sounds counterintuitive, but the idea is that there is no growth without mistakes. You must be willing to take risks and look foolish to be a successful entrepreneur. Not doing so would be, well, a mistake.

Even the best-laid plans won't work out as intended. And it's hardly an understatement to say we didn't have the best-laid plans when we started. For example, early on, one of our key metrics for purchasing properties was price per unit. Unfortunately, this pushed us to buy in rough areas we were not specialized in managing. We lost a good deal of money and suffered through even more headaches before adjusting our criteria. Business is a never-ending game of adjustments.

Of all the mistakes one of my biggest missteps was being too afraid to make mistakes. Of course, you should avoid mistakes whenever possible, but the fear of making an error is often more damaging than actually making one. There were several acquisitions we could have made but didn't because I was worried they would turn out badly.

With hindsight, I now see those acquisitions would have made for great investments. Unfortunately, at the time, while the numbers looked good, I still hesitated. The same can be said of several employees we should have let go earlier than we did. In most cases, we knew well in advance that they weren't a good fit. An inordinate amount of time was given to people who we should have never hired in the first place and then took way too much time before we let them go. But fear of making an error caused to us to keep them employed.

Never forget that the mistake of inaction are mistakes as well. This is something that many new entrepreneurs face. We all would benefit greatly from getting more involved with other, like-minded investors to keep a sane perspective and deal with such obstacles. The one mistake we didn't make was giving up. That's the only real mistake.



AMANDA'S STORY: Real Estate Meltdown to Financial Strength

July 2010 and July 2018 could not have made for a bigger contrast in my life. During that first July I received a foreclosure notice after losing my job during The Great Recession. I had bought my 2350 sq. ft. dream home from proceeds I received from another sale. Now it was all gone.

In July 2018 I purchased my second dream home, that includes a one-bedroom ADU rented for $1,000 per month. Though I completed building the home ten months earlier the bank delayed the loan. But now I had come full circle.

In my eight-year hiatus from home ownership I learned an immense amount about real estate investment. Ironically, I started working in January 2011 for Stewardship helping homeowners do short sales. It was ironic because as I helped them navigate the short sale process, I leaned how I could have done a short sale myself and avoided foreclosure (and subsequent bankruptcy) if I had been better informed.

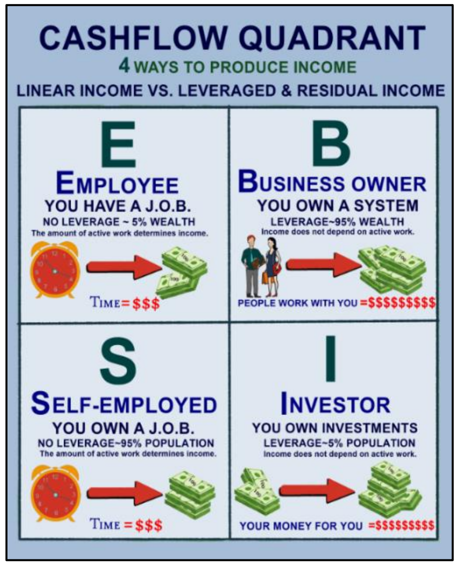
From overseeing short sales, I became our Eugene property manager, working on ways to increase rents and lower expenses to bolster our financial strength. By that time our Midwest focus took off and I took on the role of operations manager, overseeing lending from over 75 private lenders and working to help our partners purchase, rehab and rent hundreds of properties, while becoming a partner myself.

My story is one that highlights the power of knowledge. To be successful as a buy and hold investor you must carefully and incrementally build an infrastructure that employs great systems run by great people. Figuring out how much you can take on without overreaching is a constant challenge. The ride has been both thrilling and terrifying as we've grown our collective asset base to 116 million with the goal of becoming a billion-dollar company in the years to come.

RYAN'S STORY: Confession: I Am Not a… Graduate

I didn't grow up with money, nor was I around real estate investment. In fact, six months before I got started (in wholesaling) I was studying to become a police officer and planning to do the normal nine-to-five grind like the rest of the world.

Then, a stroke of good fortune. I found and read the book, *Rich Dad, Poor Dad*. By the end of it, I had found an alternative cash flow quadrant for money and wealth. But still, I didn't know what to do practically—how to build passive income. *Rich Dad, Poor Dad* taught me that I didn't have to work for money "per hour" and that money could work for me. But it didn't really teach me where or how to invest my money to make that dream a reality.



Eventually, I discovered THE KEY to making the Rich Dad's mindset a reality most effectively came from the power of real estate investing.

So, the financial trajectory of my life changed. In brief I've gone from wholesaling six properties in 2016, to 74 in 2017 to acquiring 73 rental units in 2018, with a little over 4,000,000 in cash-flowing assets and I feel like I'm just getting started with huge goals going forward.

Now this may surprise you. Although I believe and have experienced real estate as the best means to become wealthy, I still think of myself primarily as a marketing guy. I built a company (Ballpoint Marketing) that does print marketing for investors and another one (Call Porter), that takes live calls to set up appointments for real estate investors.

As someone who grew up middle class with a dad who wore the scars of hard work like a badge of honor, I inherited the belief that you had to work extremely hard for decades to build "wealth." I was wrong.

In time, my grandpa became the reason I wasn't okay with building wealth the normal way—check in, check out, retire, die. He was a medical device sales rep that traveled, busted his rear, and stacked cash for 50 years. I watched him and my grandma grow apart in his constant travel and absence. When he retired it was heart-warming to watch them gradually fall in love again. Then, a year later, she had a stroke, didn't remember his name, and he became her caretaker.

He had "passive income" when it didn't matter and worked like a mad dog when he could have been enjoying life with his family.

In contrast, I became a millionaire (okay, that's in equity and from four businesses) before my 25th birthday without graduating from high school. Now, that's an odd pedigree, but I was homeschooled from 8th grade until my mom went back to work. This unusual schooling experience gave me the crazy idea that "the rules" from the rest of society didn't apply to me, that I could throw out "the book" and do things differently. So, I did.

I have nothing, by the way, against college (or graduating from high school, for that matter!) but there's one other thing for which I'm thankful: I was able to start building wealth long before otherwise possible if I would have chosen the traditional education route. If there is any lesson here, it's this: It's never too early to start. Do it NOW!

If *Rich Dad, Poor Dad* made you feel all dressed up and nowhere to go (as it did me), the book you have before you is the antidote. We'll walk you through the specifics of what our real estate businesses do day-in and day-out to purchase properties in multiple metros at 70 cents on the dollar and then build out the infrastructures of buy/hold wealth producing companies. We've done it and so can you!

Now, how about you?

Where are you in your real estate pursuits/business?

Have you faced your fears of making mistakes? Are you embracing mistakes as steppingstones rather than the apocalypse?

Have you decided to go for it, getting ongoing training, purchased a few (or more than a few) properties, but are still wondering how to best scale-up your efforts? Are you asking yourself:

How can you most effectively and lucratively build your business?

What do you need to see happen right now to scale your business?

What is the financial story you ultimately want to write for yourself?

YOUR BUSINESS
The VEHICLE of Wealth Creation

Could I begin life again, knowing what I now know, and had money to invest, I would buy every foot of land on the Island of Manhattan.

- John Jacob Astor, American's first multi-millionaire
May 4, 1834 at age 71

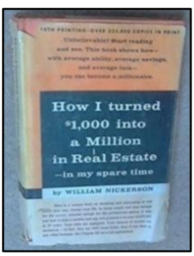
My wife, Lucille, and I came from low-income families, poor in worldly possessions. Like most of our contemporaries starting to earn a living during the depression, we were obsessed with a goal of security…. I started my pyramiding with only $1,000… reinvested on a spasmodic rather than a constant basis, and still surpassed a million [in 1959 dollars] within seventeen years.

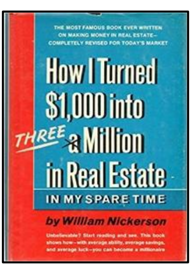
-Bill Nickerson, The Godfather of Modern Buy & Hold Investing
How I Turned $1,000 into a Million in Real Estate--in My Spare Time
Editions: 1959—One Million / 1969—Three Million / 1980—Five Million

CHAPTER 1
The I-D-E-A-L Get Rich Slow Scheme

How I Turned $1,000 into a Million in Real Estate in My Spare Time (later revised to $3 million, and then to $5 million published in 1959, then 1969 then 1980) was written by an investor named William Nickerson.

I (Bill) own all three versions, but it was my purchase of the '59 edition where I found a treasured, folded up flyer and signed note from the author himself to one of his students. Mr. Nickerson became a real estate "guru" before there was such a thing and it's fun to watch how his net worth grew (in retrospect) from zero to one to three to five million dollars during a 25-year period—and when a million dollars amounted to a LOT of money.






Dear Mr. Bodin: A more careful re-reading will show you that, beginning on page 12, Step 2, renovating is also paid for by "net income from the property." Further examples point out that improvement costs may be paid for by refinancing. Best of luck to you!

Yours sincerely,

Just Published!

JUN 16 1961

How I turned $1,000 into a Million in Real Estate— in my spare time

MY ODYSSEY AROUND THREE WORLDS (Earth, Heart & Soul)(August, 1961)

by William Nickerson

Have you ever dreamed what it would be like to be a millionaire, then told yourself to quit wasting your time dreaming? The author of this book, William Nickerson, never supposed it was possible for him either. When he started work during the depression, the most optimistic economists told him that he would be lucky to hold a steady job and retire at 65 on a small pension.

Instead, in just 15 years, working at his new real-estate projects in his spare time, he pyramided his modest savings into more than half a million dollars. Then, in his 40s, he retired to give full time to supervising his property and to enjoy gardening, travel and other recreation. He soon increased his estate to over $1,000,000.

Here is a unique book on investing and reinvesting in real estate that may change your life. In terms simple and clear enough for the novice, detailed enough for the professional realtor, it tells you how to take a modest nest egg and pyramid it to over $1,000,000 in 20 years. Your risks are negligible. Your chances of success are enormous - in fact, they are 1600 times better than if you start in any other business. The book tells you everything you need to know to make your fortune in real estate. He tells you step by step:

*how much money you can start with
*how to grow rich on borrowed money
*how to choose and buy your first property
*how to improve your property for profit
*how to trade properties to get maximum income
*how to advertise and rent apartments
*how to write effective leases
*how to collect rents
*how to handle evictions
*how to make a three-way trade
*how to hire an apartment manager
*how to refinance your holdings
*how to save on your income taxes
*how to operate under government regulations and rent controls
*how to avoid common errors
*how to make your property buy you more property

How I turned $1,000 into a Million in Real Estate —in my spare time

by WILLIAM NICKERSON

Check These Exciting Chapters

How You Can Make a Million Dollars
Buying Your First Property
How to Improve Your Property for Profit
Buying Your Second Property
Increase Value by Improving Operations
Buying Your Third Property
Managing Your Apartments
Financing Your Pyramiding
How to Save on Your Income Taxes
Developing Your Estate

W. Nickerson

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MY ODYSSEY AROUND THREE WORLDS, or

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About the author

William Nickerson is today part-time manager of his real-estate holdings. He spends his leisure gardening, fishing, swimming in his back-yard pool, playing tennis and bridge, taking part in church affairs, and traveling. He has also found time, over the past five years, to write this book. Mr. Nickerson and his wife (whom he married while he was still a student at Fresno State College) live in California. They have two children.

Such fortunes create generational wealth. For Nickerson, who passed away in 1999 at the age of 91, the story was different. Before he died he gave away his fortune. Wouldn't it be fun ride to do something similar yourself?! It's our contention that you can do just that.

William Nickerson's books not only highlight the wealth potential of buy and hold investing, they provide a model for how to grow a small nest egg into a large business with some hard work and patience. He also shows the, well, anti-miracle of inflation as the following hard-to-comprehend passages highlight:

In this case, discounting our target figure by about 5 per cent to $8,200 would represent a bargain. Increasing the $8,625 about 5 per cent to $9,000, the figure we arrived at when making our appraisal, would give us a good buy. To the target price about 10 percent might be added, making $9,500 our top price. If the offer is too low, the seller might shy off completely and refuse to negotiate without a higher starting offer. If the offer is too high, negotiations will be difficult to complete within the boundaries set. The first offer should probably be about 10 per cent less than the $8,625 we aim for, rounded to $7,750. (Nickerson pg. 75).

Good advice for sure. But those prices just sound utterly ridiculous. And then, of course, there's the rehab costs—Whoa! (And I thought I was the only one who consistently underestimates rehab budgets!!)

- *Front porch modernization and repair: 270.00*
- *Garden Transformation: 110.00*
- *Painting Exterior: 500.00*
- *Plumbing and heating modernization: 220.00*
- *Electrical modernization: 42.00*
- *Carpentry additions: 83.00*
- *Tile and linoleum rejuvenation: 170.00*
- *Painting and decorating interior: 375.00*
- *Furniture and furnishings: 27.50*
- *Plumbing Repairs: 27.60*
- *TOTAL for Rejuvenation and Repairs: $1,826.10* (127-128)

The Ultimate Get-Rich-Slow Scheme

Anyway, while some of his advice—such as how to scroll through classified ads in the newspaper for deals or valuing single family rentals on their net income instead of their comparable sales (it was a bit harder to run comps back in the day)—is a bit antiquated, his overall recommendations are still very relevant.

William Nickerson's strategy was essentially to pyramid from a small property into a larger one and then to an even larger one and so on using the built-up appreciation, principal pay down and cash flow. Here's how he describes a path like what made him a millionaire (back when that meant a lot more than today):

ZERO DAY… You take the $2,500 nest egg from your savings account. Then you borrow three times as much, $7,500, making a total of $10,000. With the $10,000 you buy a rental house in need of renovation…

…TWO YEARS… You sell the improved house for $14,000 [receiving $5,800 back]… You take the $5,800 and again borrow three times as much, $17,400… With this you buy a 4-unit rental-income building…

…FOUR YEARS… You sell the improved 4-unit building… this leaves you a profit of $11,575…[Then invest that] in an 8-unit income-producing property… (25-26)

And so on and so forth. While these numbers might sound small, by compounding it in this way, by the 20th year, your total net worth would be $1,187,195. (See for yourself.) It took Nickerson 17 years. Wasn't it Albert Einstein who described compound interest as the "eighth wonder of the world"?

Scaling Up Your Real Estate Business

The author then illustrates the process by describing the purchase of a single-family house and moving up to a five-unit and then a 24-unit and so on. Back then, trades were quite common, even complicated three-way trades that reminds you of trades between NBA teams. For example, he describes trading the house and some money for the five-unit apartment.

Nowadays, such trades are rare, especially for houses. But it's similar to the BRRRR method; namely, *buy, rehab, rent, refinance and repeat*. Sure, you can sell (or even trade) your properties to move up, but why not simply refinance them, continue to hold them, then another, then another, and then another?

Beside promoting a type of BRRRR method, the important thing that Nickerson's story shows is to keep the long-term perspective in mind. Buy and hold can often feel like a slow, never-ending grind to simply scrape by. In the beginning, there's a lot of work for just a little cash flow. Indeed, one metric we use is that any house we buy must cash flow at least $100 a month and an apt unit, $50, while fully financed. But if you think about that, $50-$100 a month doesn't go very far.

Even with 10 such properties, you're making maybe $1,000 a month, which is nowhere near enough to live off of or to build a business. (Of course, that includes all expenses and being fully financed; they cash flow much better with less or no financing.)

IDEAL Compounded Advantages

But the cash flow itself is just one of the many. Cash flow only covers the "I" of the I-D-E-A-L acroymn that portrays the advantages of buy and hold real estate investment. Here's the others:

I: Income / **D:** Depreciation
E: Equity Buildup / **A:** Appreciation / **L:** Leverage
(Plus, another **I:** Inefficient Market)

These multiple advantages begin to compound on themselves, and your growth slowly but surely becomes exponential. Sooner or later, it just hits you that you've made it and that you've built a great portfolio of cash flowing assets and a sizable income to boot. Many years after I (Bill) started in Oregon, I had this very epiphany, and later in

Kansas City, my son’s Andrew and Phillip had the same, surprising experience: we’re millionaires! But it certainly doesn’t happen overnight.

In the end, the lesson is to beat into your mind that real estate investment, particularly buy and hold, is a *get-rich-slow* scheme. It may feel like a long, arduous climb. But trust the numbers and the system that those who came before us, such as William Nickerson, used. You will get there. It just takes hard work, time and a sizable slice of patience.

So, this is the ultimate get-rich-slow scheme, and nothing could highlight that more than William Nickerson’s career. Indeed, be prepared not to “buy and hold” but to “buy and survive…until you thrive.” However, if you can “hold” long enough, thriving means, you end up rich!

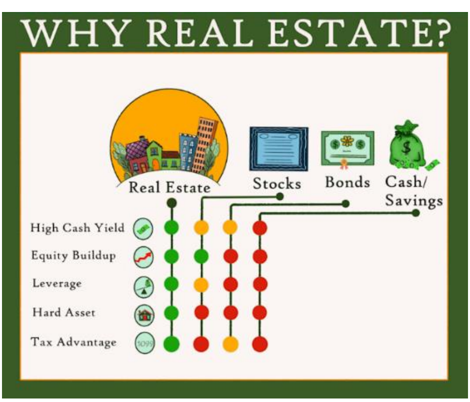
BUY & HOLD INVESTING: It’s I-D-E-A-L

Let’s start with the last letter of I-D-E-A-L: leverage. Real estate is an investment that can make a person of average means wealthy due in large part to leverage. Leverage allows us to control hundred-dollar bill with a twenty (20% down payment) or a ten, five, one or even none and sometimes with less than none—we are paid for the privilege of owning a piece of property!

You can look no further than the playground for a good illustration of leverage, especially the tetter-totter. Where else can the weight of a full-grow adult be controlled by a small child? It's all about where the fulcrum (point of leverage) is placed between them. Leverage is the ultimate enhancer.

When you use only a small portion of your own funds (or even none of your own money) to purchase and hold a property, you still gain all the benefits of the whole property's value. So, if you buy a property with 20% down and the property's value goes up 5%, you make a 25% return from your value-add or appreciation because your down payment is now worth 25% more than what you invested even though the property only went up 5%. All of this doesn't come automatically, but where else can you make an annual return of 25% for doing so little?

Be aware that just as leverage can work for you, it can also work against you. That's why buying at a discount with a safety margin is so important. We'll take up this subject again.



Bottom-line, there are precious few investment instruments that allow for leverage in business or investing and this gives real estate a rare advantage that only those who own it enjoy. This is why most, some say as high as 90%, of the country's millionaires, have made their money through real estate. No other investment they own can compete with its benefits. For a comparison of stock market returns to real estate, check our this article.

Not only does buy and hold real estate investment provide the benefit of leverage, it is the all-around IDEAL business investment. Why? Let's define the letters: **I-D-E-A-L**:

I – Income from rent which should equate to positive cash flow.

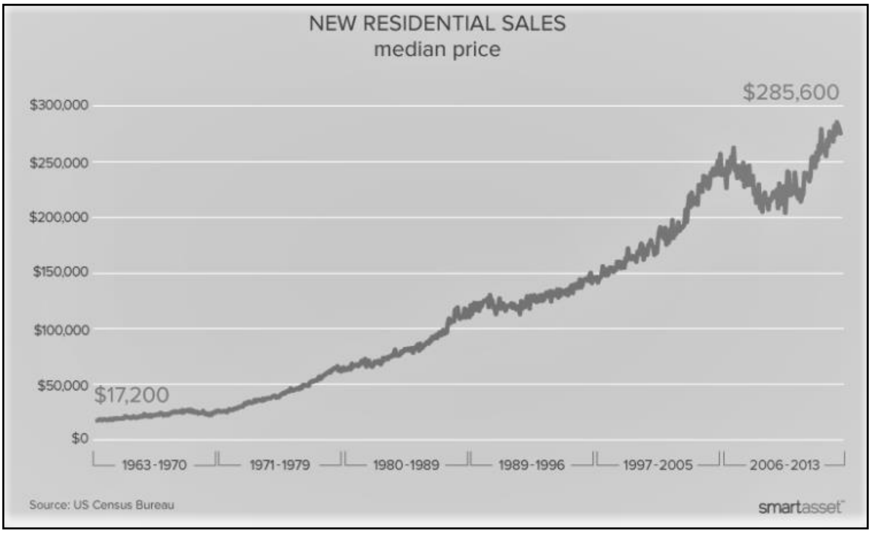
D – Depreciation as an ongoing tax benefit of holding property.

E – Equity Buildup from paying down mortgages over time.

A – Appreciation broadly follows the long-term 3.24% inflation rate.

L – Leverage using other people's money to enhance returns.

Though real estate has its ups and downs, over time it has seen an upward trajectory of value at about the rate of inflation



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A rather sad example of not taking this graph seriously: I hate playing the woulda, coulda, shoulda game, but indulge me for a moment.

Sitting in front of my laptop in the late '90's, I (Bill) remember looking at Apple stock for $23 (it actually went further down to $15). If we could go back in a time machine and buy Apple right after Steve Jobs came back to the company, would we? Of course! After stock splits, a $23 stock would now be worth around $2,180 today. You can do the math: 1,000 shares would now equal $2.18 million, 10,000 shares would equal $21.8 million (AppleStockValue). I don't lose sleep over this "loss," because how could I have known that Steve Jobs would so masterfully turn Apple around? (Note to self: we've actually had a better return, an *infinite* one, because of being able to build our real estate portfolio with none of our own money.)

Now back to the story: I had no control over what was happening inside Apple's headquarters in Cupertino, CA, but I did have control over another situation. I had bought a home in an upscale Mt. Tabor Portland neighborhood in the early '80s for $60,000 and rehabbed it. I was just starting to get into real estate and didn't have a game plan. Not wanting the burden of figuring out property management or financing another deal, I decided to sell it. ("Flip it" would imply I made a profit, so I'll stick with "sell it!") A couple named Michael and Julie bought it for $70,000.

A number of years ago we crossed paths by chance and chatted about the Portland housing market. During the recession in the mid-80s, I found out that they had sold the house at a loss for $66,000. Michael asked if I wanted to know about its most recent sale. "I don't want to know," I replied. Ignoring my petty objection, he blurted out, "$950,000!" As of today, it has since appreciated another 35%+, meaning the house I sold for $70,000 35 years ago is now worth $1,212,500 more than my selling price!

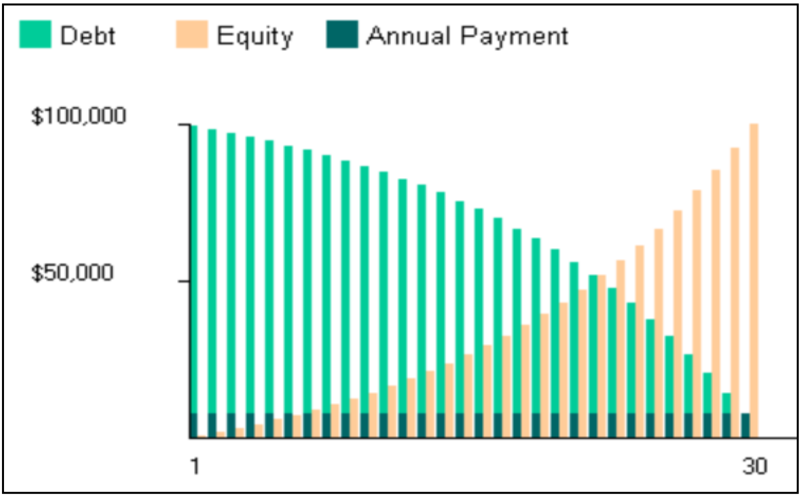
Congratulations to whoever made a whole lot of equity/money; that whoever wasn't Michael and, of course, it wasn't me either. What if, instead of selling, I would have figured out how to navigate management and financing issues, then doubled down, tripled down or better yet, bought another 10, 20 or 30 of those Portland homes?

We can't go back in time, but time is certainly going forward. Do you think 10, 20 or 30 years from now that buy and hold real estate investors will look back with regret, and say woulda, coulda, shoulda? We doubt it, although those who sit on the sideline likely will, as could flippers. Why? Because simply put, buy and hold real estate investment is the **I–D–E–A–L** (plus we'll add an additional "**I**") investment.

I – Income: Unlike bonds and most stocks, real estate provides monthly income in the form of rent. Buy and hold, when done properly, brings in positive cash flow each month, creating a residual income stream that works for you no matter where you are or what you are doing. It's passive income.

D – Depreciation: One of the cons of flipping is that it produces taxable income at ordinary rates whereas holding real estate can potentially allow you to have an income but show a loss on your taxes from depreciation. Thus, buy and hold can provide a reduced or non-existent tax burden and any refinance provides tax-free capital.

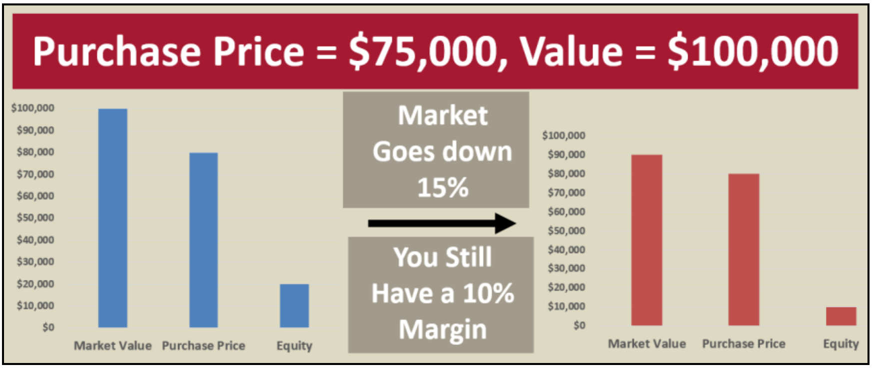
E – Equity Build Up: Unless the mortgage is interest-only, each payment made on the loan cuts down the principal. In effect, you are using the rent to pay off the mortgage. Amortization tables are a thing of beauty to buy and hold investors because each month they get closer to owning the property debt-free and then increase cash flow drastically. Or, along the way, the investor can refinance and pull out a chunk of that equity for new investments.



A – Appreciation: While each region/area/city/neighbor real estate market is affected by supply and demand, since 1913 real estate prices have generally followed inflation which has appreciated at 3.24% a year. The 2008 housing crisis made it clear that depreciation also exists. However, the buy and hold investor is all about cash flow and can ride out bad real estate markets (and even buy in downward markets when properties become cheaper).

L – Leverage: And, we're back where we started, with the benefit enhances and outweighs them all…literally.

All real estate is local, so values move with the supply and demand dynamics of a region, area, neighborhood, even street. Be prepared for market downturns by always buying with a margin of safety. A property purchased 25% under its market value will still have a margin if its value goes down 15-20%. And, in the final analysis, we are cash flow investors, so it is the rental income which we are most sensitive.



Dollar-Cost Averaging Applied to Real Estate

Dollar cost averaging is used to describe a stock buying plan when a stock buyer purchases, for example, $5,000 in stock per quarter. When buying properties over time we also dollar-cost average. The idea is that the first properties purchased years ago are more valuable now and make up for those bought more recently that don't have as much value or profit margin. Real estate purchases over time provides a key to building a safety margin within your portfolio now and later.

Adding a Final "I," to I-D-E-A-L…I:
Real Estate is an—Inefficient Market

It's difficult, unless you have insider information (can you spell illegal), to make a great deal in the stock market upon purchase. Why? Because thousands of other investors have the exact same information available to them as you do in make their stock buying decisions. Thus, the stock market is a very "efficient" market.

On the other hand, each real estate transaction is different. There is a unique seller, a unique property in a unique condition, unique circumstances, a unique buyer. Did you catch the repeated adjective here?! It is this unique inefficiency that provides opportunity to the investor.

Through finding a motivated seller, quality negotiation skills and with value-add measures (upgrading, changing use, raising rents) real estate may be uniquely "enhanced" to add more value and cash flow than the capital and time required to make those enhancements.

An inefficient market allows investors to buy under market (less than the property is worth) or under potential (less than the property could be worth with value-adds) if you are willing to hustle and negotiate.

Granted there are other places that provide inefficient market opportunities, like garage sales. But last time we check a garage sale doesn't offer the other I-D-E-A-L factors that real estate does, especially when you're getting 50 cents off on that dollar leather belt!

Get Rich…Slowly

Occasionally real estate turns out to be a get rich fast scheme—it is, after all an inefficient market out there and crazy, incredibly profitable deals happen all the time. But patience is the key virtue here.

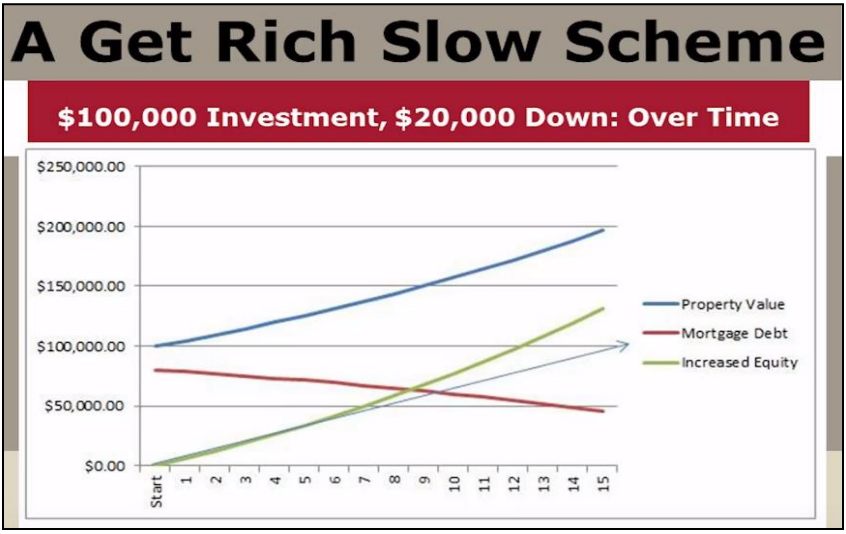
The I-D-E-A-L…I wheel turns slowly, making you equity rich yet cash poor especially as you begin paying to build out its necessary infrastructure. If, however, you work the system, over time you will create more wealth than you ever imagined. Just get great deals and keep a lid on expenses (we'll talk about each) and you'll have no regrets.

While flipping brings in a profit (hopefully), once a property is sold the benefit is gone and, unless you 1031-it, your liability begins in the form of taxable income. Buy and hold is cumulative and exponential with abundant tax benefits. Just follow the description below and look how it is portrayed on the graph. As your portfolio grows, so does the compounding factor behind these related benefits.

If you buy a property for $100,000 with an 80% LTV (loan-to-value) loan at 5.5% interest to be paid back over 25 years with $20,000 as a down payment. If it appreciates at 3.24%, the equity you have in the property (over your initial $20,000 investment) goes up exponentially. After five years, you have an additional $25,000 of equity.

After 10 years, it would be $57,000, and after 15 years you have $96,000 in additional equity. The annualized return on your investment starts at 23.9% (not bad), but by year 15, it has gone up to almost 32%! And that doesn't include positive cash flow or paying down the loan. Plus, your return is even better if you had purchased at wholesale rather than a retail price. If you refinance it and receive back your $20,000, you would have an infinite return!

Multiply this with additional properties and you've become a modern-day version of William Nickerson.



The Challenges of Buy and Hold Real Estate Investment

All this said, buy and hold is not for couch potatoes, unless of course, you're on the couch searching for your next great deal. For anything that has the kind of I-D-E-A-L…I benefit just described there have got to be serious challenges; otherwise, everyone would be doing it. Right?! There are others, but here are four main challenges:

1) Finding the capital to start the process and to keep buying.
2) Marketing for great deals to purchase below market prices.
3) Overseeing rehab crews for maximum value, minimum cost.
4) Building out, overseeing and paying for the systems and team infrastructure to manage your properties on a long-term basis.

Rent-to-Cost Ratios Show Which Properties Work for Buy/Hold

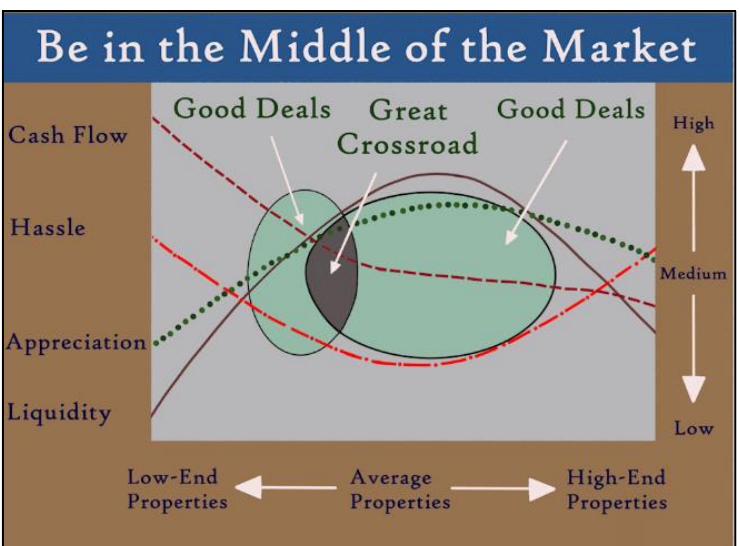
Our goal is to acquire, rehab and rent properties 20% under market value (preferably 25-30%) with a minimum of a 1% rent-to-cost ratio in working class areas (.75% in more expensive markets) that are not too difficult to manage. The rent-to-cost ratio is calculated by dividing the monthly rent by the purchase price.

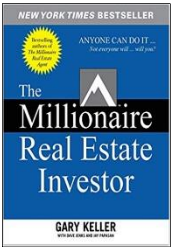
Property Value = $100,000—Rent-to-Cost Ratios

.75% = $750/month rent
1% = $1000/month rent
1.25% = $1,250/month rent
1.5% = $1,500/month rent

Low-end markets can generate as much as a 1.75-2% rent-to-cost ratio, but such attractive numbers usually come with run-down properties and very challenging management issues that most investors would do well to avoid. Some regions and markets generate no more than a .5% rent-to-cost ratio, forcing investors to set their sights on flipping, hoping for appreciation or looking out of their area or out-of-state for their buy and hold purchases. All these factors should help us determine our target market(s).

As expected, there are pros and cons within every market class. In *The Millionaire Real Estate Investor*, a modern classic, Gary Keller et al, identifies four broad real estate investment factors to consider as you target a market class: 1) cash flow, 2) appreciation, 3) property management hassle, and 4) liquidity. Each factor rises or falls depending on the value of a property, its price and location, as visualized in this graphic adapted from page 187 of his book. Note the "sweet spot."





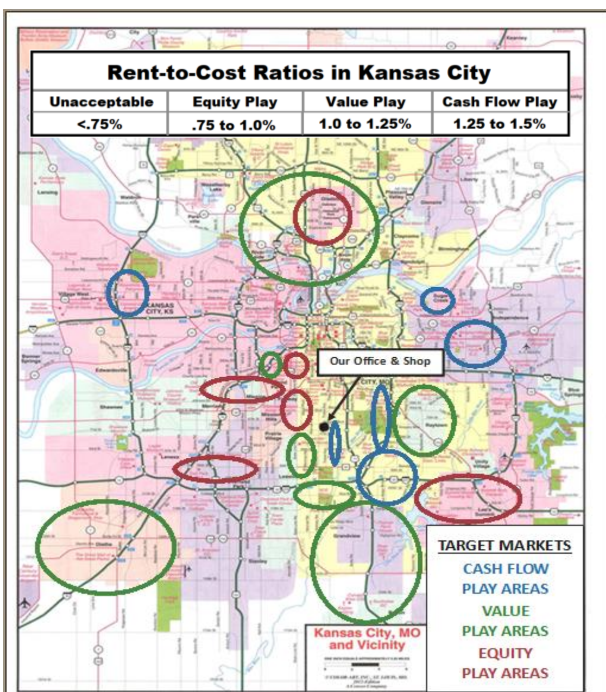
The author suggests it's best to *Be in the Middle,* where most renters rent and most buyers buy. These are the bread and butter properties in most markets. Keller specifically directs buy and hold investors to go after the "great deals" as he puts it, or maybe better put, the "great crossroad") of lower-to-middle valued properties as the previous graph identifies.

When you buy in the rent-to-cost "sweet spot" you will:

1) Avoid illiquid, low-end "war zones," yet still
2) Find solid, cash-flowing deals (with a high ROI), and a
3) Reasonable amount of property management challenges, with
4) Relatively good prospects for value appreciation.

The map identifies three targeted Kansas City sub-markets: 1) lower (cash flow plays), 2) lower-middle (value plays) and 3) middle (equity plays) with the rent-to-cost ratios in each of these submarkets.

We buy properties in each of these three categories to get a mix of them and their benefits to our portfolio:



Cash Flow Plays: Lower areas. Best cash flow, harder to manage.

Value Plays: Lower middle areas. Decent cash flow, better locations.

Equity Plays: Middle areas. Less cash flow, more likely to appreciate.

Are Your Numbers Right? 11 Helpful Calculations

Despite what many of us math-allergic folks would prefer, real estate does involve some math. Luckily, most of the formulas are simple and straightforward. In fact, if you understand the 11 calculations below, you'll be in good shape. (**The calculators:** thinkrealty.com/calculators)

#1: Rent-To-Cost *Monthly Rent / Total Price of Property* (All-In)
Example: Monthly Rent: $900
Total Price of Property (Purchase + Rehab): $75,000
Rent/Cost = $900 / $75,000 = 0.012 or a 1.2% Rent/Cost

Let's revisit this helpful calculation for houses and even small multi-family apartments. Note that it should only be used when comparing the rental value of like properties. Do not compare the rent-to-cost of a property in a war zone to that in a gated community. A roof costs the same, per square, in both areas. Vacancy and delinquency will be higher in a bad area, so rent-to-cost won't tell you what your actual cash flow will be. But when comparing like properties in similar areas, rent-to-cost is a very useful tool.

According to Keller in *The Millionaire Real Estate Investor*, the national average rent-to-cost ratio is 0.7%. For cash flow properties, you likely want 1% or above. As mentioned, in Midwestern and Southern markets we aim for a 1.25 depending on the area—in higher priced areas it will be more like .75 to 1%. And yes, we would recommend having a target rent-to-cost ratio for any given area.

#2: Gross Yield (GRM) *Annual Rent / Total Price of Property*
Example: Annual Rent: $9,000
Total Price (Purchase + Rehab): $100,000
Gross Yield = $9,000 / $100,000 = .09 or a 9% gross yield

This calculation is similar as rent-to-cost but reversed. It's used more often when valuing large portfolio, but overall, it serves the same purpose as rent-to-cost. (A 1% rent-to-cost ratio equals an 8.33 GRM.)

#3: Gross Rent Calculator: Sale Price / Gross Annual Rents
Example: *Sale Price = $500,000* *Annual Rents = $50,000*
Gross Rent Multiplier = 10 ($500,000 / $50,000)

You can use this calculation (for just sales price or total cost including rehab) when looking for a quick sign a potential commercial deal (multi-family or otherwise) is worth considering. It is limited because it doesn't take operating expenses into account.

#4: Cap Rate *Net Operating Income / Total Price of Property x 100*
Example: NOI (Net Operating Income—Inc. after expenses): $25,000
Total Price (Purchase + Rehab): $300,000
$25,000 / $300,000 = 0.083 x 100 is an 8.3% Cap Rate

This calculation is mostly used for valuing apartments and larger commercial buildings. It can potentially be used for houses and small multi-family units too, but operating expenses are erratic with houses because you don't know how often and how bad turnovers will be. Also, houses are sold more to homeowners (who are willing to pay more for their personal residence) than investors thus increasing their value above just their rental income potential.

You want to have a cap rate that is at least as good, preferably better, than comparable buildings in the area. We almost always want to be at an 8% cap rate or better, although in some areas, that's not really possible. And always be sure to use real numbers or your own estimates when calculating this. Do not simply use what's on the seller provided pro forma. Call them by their real name: "pro-fake-as".

#5: Debt Service Coverage Ratio *Net Operating Income / Debt Service*
Example: NOI: $25,000 Annual Debt Service: $20,000
Debt Service Ratio (DSCR) = $25,000 / $20,000 = 1.25

This is one of the most important numbers that banks look at and is critical for getting financing. Generally, a bank will look at both the property's debt service ratio and your "global" debt service ratio (i.e., the debt service ratio of your entire company or portfolio).

Anything under 1.0 means that you will lose money each month. Understandably, banks don't like such a skinny contingency and you shouldn't either. Most lenders will want to see at least a 1.2 DSCR ratio or better (your income equals 20% more than all your expenses including mortgage). In that way, you have a cushion to afford the payments in case something happens that leads to a decrease in rental income or an increase in expenses.

#6: Cash-on-Cash *Cash Flow / Cash into Deal*
Example: Cash Flow (Net Operating Income – Debt Service): $10,000
Cash into Deal: $40,000
Cash on Cash: $10,000 / $40,000 = .25 or 25%

In the end, this is the most important number. It tells you what kind of return you are getting on your money. In the above example, if you had $40,000 in the deal and made $10,000 that year, you made 25%. This is a critical calculation not only when it comes to valuing a property, but also when it comes to evaluating what kind of debt or equity structure to use when purchasing it.

#7: The 50% Rule *Operating Income x .5 = Probable Operating Expenses*
Example: Operating Income: $100,000
Operating Expenses = $100,000 X 0.5 = $50,000

This is a shorthand rule that we judge to be ok. It is for estimating the expenses of a property. Whenever possible, use real numbers (i.e., the operating statement), but this is good for filtering out deals that don't make sense. Just remember, a nicer building will have a lower ratio of expenses to income than a worse one and other factors, like who pays the utilities. Just don't rely on this rule.

#8: The 70% Rule *Strike Price = (0.7 X After Repair Value) – Rehab*
Example: After Repair Value: $150,000
Rehab: $25,000
Strike Price = (0.7 X $150,000) – $25,000 = $80,000

This is like the 50% rule and helps for coming up with an offer price. Always crunch the numbers including closing and holding costs before purchasing. But if you offer off the 70% rule, you should be just fine if your rehab estimate and ARV (after repair value) estimate are right.

#9: Return on Investment (ROI)

(Gain on Investment – Cost of Investment) / Cost of Investment
Example: *Gain on Investment = $20,000*
Cost of Investment = $50,000. Years owned = 5
ROI = 40% ($20,000 / $50,000)
Annualized Return (AR): ROI/# years you owned the property
AR = 8% (40%/5)

ROI gives you a "whole picture" of a future or completed investment. It helps an investor anticipate the return of a particular investment and thus its attractiveness when weighing the risk involved.

#10: Internal Rate of Return (IRR)

IRR is defined as "the discount rate that makes an investment's net present value equal to zero." IRR accounts for when you spend and receive cash. Usually it is better to receive cash sooner rather than later because then you can reinvest it. You will need an IRR calculator (our favorite is the IRR function available in Excel) to derive it.

When to use it: To put your ROI in perspective with your initial outlay of money or compare investment opportunities in different asset classes. It omits external factors such as cost of capital and inflation.

#11: Comparative Market Analysis

There is no real calculation for comparative market analysis. It's used for house hunting to find similar properties then make adjustments to (close to) identical values (or with multifamily or commercial properties comparing sq. ft. values). The MLS is by far the best for this, but Zillow and Redfin can work too (just don't rely on the Zestimate).

For complimentary calculators see: thinkrealty.com/calculators

PART 1
YOUR CORE BUSINESS

Don't wait to buy real estate. Buy real estate and wait.

-Will Rogers

The best time to buy a house is always five years ago.

-Ray Brown

Owning your own home is not a sign of wealth. Owning someone else's home is. -Unknown

Ninety percent of all millionaires become so through owning real estate. More money has been made in real estate than in all industrial investments combined. The wise young man or wage earner of today invests his money in real estate.

-Andrew Carnegie

CHAPTER 2

PLAY "THE GAME" OF REAL ESTATE WEALTH CREATION

I (Bill) have been playing this game for 40 years (and started Stewardship in August, 1989). Yet I often feel like a newbie. This is because real estate and business building is so big and broad, with multiple niches and strategies that demand personal and business growth. I'm learning something new and being challenged every day. So, let's first consider two key qualities for business success: *Humility* & *Hustle*.

HUMILITY leads to Teachability and Growth

Are you open to learn, but even more than this, are you a learner? Are you actively looking to increase your knowledge basis and skill level?

Awhile back I met Michael, an eager would-be investor who said he wanted to "get into real estate." I said I'd sit down and teach him if he'd do three things for me: 1) read ten BiggerPockets.com articles and do a "book report" on them, watch five real estate YouTube videos and do a report, and read one book you'll hear more about: *The Millionaire Real Estate Investor,* and do, yes, another book report.

A few months after that conversation I ran into Michael again. He said, "Oh yeah, you wanted some book reports, right?" *When the student is ready, the teacher will appear*…but not before! Who is your mentor and those who you can save you countless hours because they've "been there, done that?" What are you prepared to do to learn?

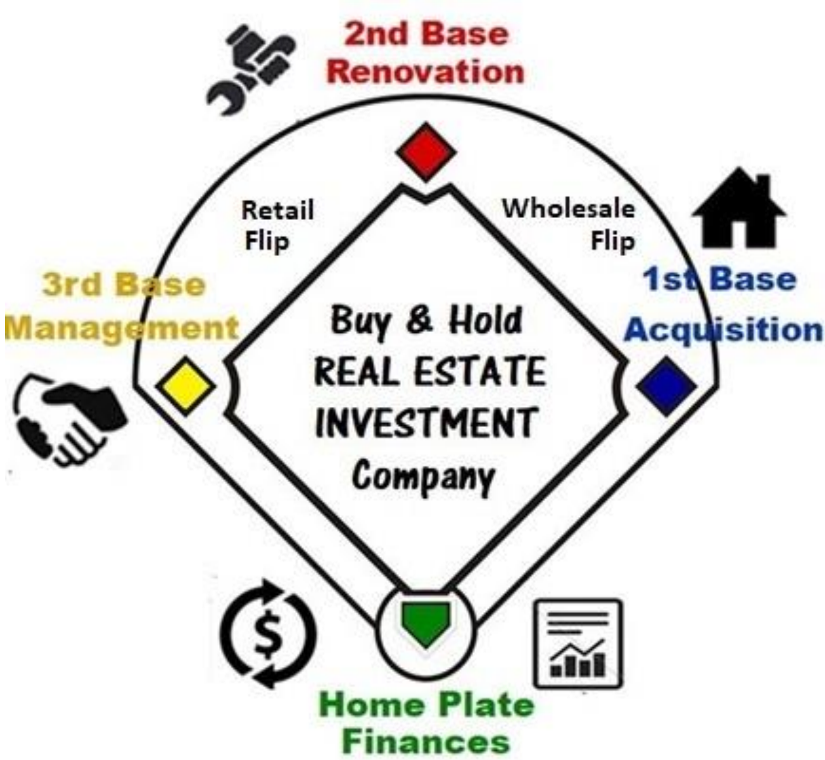
HUSTLE leads to Accomplishment and Success

Unless you have a lot of money (and that could put you into more of a passive role) the second critical ingredient is that you've got to get up from your study (or wherever you "learn") and start doing and doing big. There is just no substitute for getting after it. How many properties have you looked at this week? How big is your funnel from which your property investment options come? How many offers did you make? The most important word in the real estate investment world, indeed in business, is EXECUTION. So, *LET'S GET AFTER IT!*

So, in a nutshell, what is this "game" we're playing?

Are you a baseball fan? I am, at least briefly, during the World Series!

When explaining how our business model works, baseball makes for a good analogy. While wholesaling gets halfway to 2nd and retail flipping gets you halfway to 3rd, buy and hold investors run the bases all the way back to home plate. Our aim is to hit every good pitch from a motivated seller, round the bases and get back home, repeatedly!



START at HOME PLATE: FINANCES/private lenders & accounting

1st BASE: ACQUISITION/marketing for lead generation/purchasing

2nd BASE: RENOVATION/project management of rehab & turnovers

3rd BASE: MANAGEMENT/marketing/leasing/resident relations

RETURN to HOME PLATE: REFINANCES/bank lender relationships

How to make Flipping a Compliment to Holding

While flipping makes a profit (hopefully), buy and hold investing CREATES A FORTUNE. Buy/hold begins at Home Plate with securing financing (from a cash source, seller financing, a bank loan or a private lender), then on to Acquisition (1st Base), next Renovation (2nd Base), then Management (3rd Base) and finally back to refinancing (Home).

If our initial financing came at good terms and we don't necessarily need to refinance and recapitalize, we can stop there. But we have another option when advantageous, and that is to refinance our front-end financing with the lowest possible, long-term interest rate financing available which is often capital from a local or regional bank.

This is our secret formula for true wealth creation. Okay, it's not so secret, it's just not that widely done and done well. But, as those looking to build a mountain of passive income, this is our lifelong investor challenge and provides the foundation of building a business that produces substantial wealth and greater opportunities.

Flipping Regret

I (Bill) have regretted every property I've sold and there were many. Maybe I should say I've regretted *almost* every property I've sold. In the early days keeping my fledgling real estate business alive was the paramount priority. But after that I've regretted nearly every flip. Why?

Because of I-D-E-A-L which has meant my goal of substantial real estate wealth creation took that longer to attain—just reread page 24! Recently I was seeking to talk a "young flipper" from into trying out buy and hold and these words came out of my mouth: "If I had kept every property I've owned I'd be worth north of 100 million dollars today."

I checked myself and thought for a moment, "Is that really true?" After running through some numbers, I'd have to say, "yes, I believe it is." Before allowing a big wave of regret to wash over me I accessed another thought: "Thankfully, I kept hold of many of them!"

So, why would you ever flip? My short answer is only flip if you know it leads to buy and hold. But maybe I should lead you flippers out there more gently out of troubled waters. So, here's my thought on flipping.

Flip if it's a means to an end, for a higher purpose, like providing the necessary cash to do buy and hold. Some follow the 1-2-3 strategy: flip #1 for the down payment to flip #2 for the means of holding on to #3. Two investors I know in Salem, Oregon, Jon and Eric, did just this and now they've move on to the 1-2 strategy: buy one to flip, then buy the second to hold, and repeat.

Another reason to flip is if the property just can't cash flow. We particularly run into this issue in more expensive locations around the country. Feeding a property (covering its expenses with funds beyond its rental income) can lead you down a dangerous path.

Buy and hold investors are positive cash flow sensitive and for good reason. If you think, however, appreciation is in your future, maybe it would be wise to bring in a well-heeled partner willing to take on the negative cash flow for a piece of the equity. Just a thought.

Our partner, Ryan Dossey, says: *Keep the best and wholesale the rest.* His strategy acknowledges there is plenty of "junk" out there that can get caught up in your acquisition dragnet. Flip undesirable properties while you keep your eye on the prize of holding the best.

You can purchase the property before flipping it, even if it's a sale to another investor. This allows time to find the buyer who is willing to pay the most and it allows him to avoid the sometimes awkward situation of keeping the original seller in the loop during his contract assignment to the eventual buyer.

Flipping the Contract

However, it is also possible to flip the property before you get to 1st Base by putting the property under contract and flipping the contract. The reason to flip the contract is to stop short of buying the property yourself. This allows you to avoid closing and holding cost and the need to raise the necessary capital. I (Bill) decided to flip a property once because it was owned by a painter who built a huge attached garage and filled it to the brim with all kinds of nasty, toxic supplies dating back thirty years. Flipping the contract meant that my name was never in the chain of title and no liability could come back on me for cleanup.

If you plan to flip the contract be aware of the time constrains of your close date with the seller and include language in the contract that allows you to sell it before purchase. Such language identifies you as the buyer plus an additional phrase (which should go in all your contracts): *"and/or assigns."* This gives you ultimate flexibility to have another buyer (that comes from a buyer's list you are creating) who you're flipping the contract to (or partnering with) to step into your place as the buyer without rewriting and resigning the contract.

To Wholesale? Wholetail? or to Retail? Those are the Options.
A buying/flipping strategy comes down to making an assessment you need to make at 2nd Base or well before you get there. The only reason to "retail" a property is because you expect to realize more profit than "wholesaling" it. After the fact, we've at times concluded the time and expense involved in rehabbing a property to get top dollar, was not time and money well spent. We would have sometimes been better off, maybe even much better off, wholesaling it for "bottom dollar." Wholetailing offers a middle ground of doing some minimal upgrades.

So, the decision to flip wholesale or flip retail depends on an equation of weighing your profit potential, your rehab crews' ability and availability, your time and the cost of funds. Effective management of your rehab projects are the key to a successful retail flip, including:

--Know what your "cost per day" is. Each day the expense cost keeps ticking. Time is money and you should have a feel for how much.

--Stay on top of the project, keeping it well organized with contractors and your employee crews coming and going like a well-oiled machine.

--Constantly weigh the cost between using your own time, more skilled contractors and (often) less skilled employees.

--Evaluate buying equipment, vehicles, a shop and other items that could save you more in the long run.

--Always add a contingent fee for cost overruns and for holding cost, the secret expenses that can wreck your bottom-line.

"Yes, but how do I hold properties in expensive markets?"
We are sympathetic to this challenge, having started in Eugene and also buying properties in markets such as Portland and Austin. Below are "holding alternatives," some maybe more feasible than others.

Move to the Midwest or South (or another, more affordable market). Okay, this is kind of radical but people, including my second and third sons, Andrew and Phillip, have done it. Granted they were in their 20's when they did but it has allowed them to build a sizable portfolio of rentals that would have been very difficult in more expense markets.

Look out of State/Out of Area
A fellow investor friend, Joe, lives in an expensive area, Bend, Oregon. To apply a buy and hold strategy he has focused on Akron, Ohio and now owns 13 properties there with an average value of $30,000 and average of $735 per month rent. These properties are not in war zones, but Joe has had to oversee his management carefully. I would not advise such an investment strategy, but it could work for you.

Likely a better strategy is to focus closer to home but in a city or area outside more expensive areas, maybe smaller communities beyond the metro area or a lower cost area of town on the rise. And you can always look for a like-minded partner who can bring deeper pockets to deal with some negative cash flow to keep your cashflow at par.

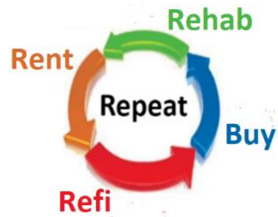
Find Local Value-Add Niches

There are value-add options that investors walk by every day which can make the difference between holding on to a property rather than having to sell it. Open your eyes to these value-add opportunities like adding bedrooms to student rentals, duplexing corner lots, finding properties with an additional lot, adding a "grandmother-in-law apartment, Airbnb'ing the property for increased cash flow to name a few.

It's all about finding ways to add rental cash flow and value to a property which allows you to hold on to it. Take a moment right now and think of every value-add possibility that makes sense in your market and, when you get a chance, listen to my (Bill's) BiggerPockets.com podcast interview, #140: youtube.com/*The-Riches-are-in-The-Niches*

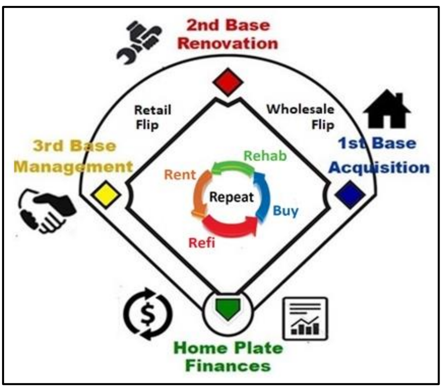
How "BRRRR" Relates to Our Baseball Diamond

Buy—Rehab—Rent—Refinance—Repeat



If you haven't discovered BiggerPockets.com, you should. If you have, you've likely heard about BRRRR, a real estate buy and hold acronym. While a baseball diamond makes for a better analogy, BRRRR makes for a memorable acronym, so we'll include both because they describe the same process.

B—Buy…Repeat (1st BASE)



They say you make your money when you buy, and that's true. The key to remember when buying properties you plan on holding is that there isn't a great feedback loop. Yes, you can get an appraisal, but you may disagree with that appraisal. Who is to say whether you or the appraiser is right? It's not a sale.

When you are flipping, you will always know how well you did because you can compare your profit or loss after the sale. When holding property, you can deceive yourself into thinking the appraisal just wasn't any good or you can leave "leave money in the property." In other words, there is a tendency for buy and hold investors to get lazy.

The goal behind a BRRRR strategy is to pull all the money you put into a property out when you refinance it so that you effectively bought a property for nothing, but still have 25% built-in equity to reduce risk. So, while you may be looking for a different type of property (flippers usually buy more expensive properties than holders), you want to get the same equity margin or close to it.

Flippers use the 70% rule as their guide in this formula:
After Repair Value (AFR) X 0.7 – Repairs = Maximum Purchase Price

Most lenders will finance 75% of the appraised value (a few at 80%), so likewise holders should aim for 70-75%. We generally do this, but we have built up years of equity so we can leave some money in our deals. Also, we are looking to buy in volume, so we are open to a buy and hold property appraising for 80-85% of what we have into it. If this does not apply to you, I would argue you should proceed more cautiously and stick closer to the 70-75% guideline for two reasons:

1. ***Refinancing costs money.*** Most banks charge a half to a point, and there are costs associated with appraisals, title work, and loan processing fees that reduce your margin.

2. ***Aiming for 75% offers no contingency.*** Investors go over budget more often than not; especially with holding costs, so building in margin is important unless you have extra assets. We are focused on volume, so we aim for 75%, but, over time, our all-in costs average about 82% of property value. Ideally, however, we aim to pull out all our cash in a refinance.

To purchase the property up-front, you can use cash, a hard money loan, seller financing, private loans, etc. These different upfront financing options result in different acquisition and holding costs. You need to account for those when analyzing a deal to hit that 75% goal. Then there are also the back-end costs of refinancing to consider.

R—Rehab (2nd BASE)

There are two questions to keep in mind when rehabbing a rental:

1. *What do I need to do to make this house livable and functional?*
2. *Which rehab decisions will add more value than their cost?*

Unless you are doing semi-luxury rentals, generally speaking, things such as the following are not necessary and will cost much more than either the rental income or property value they will produce:

- Granite or Quartz Countertops
- New Hardwood Floors
- High-end Stainless-Steel Appliances
- Compilated paint color schemes
- High-end light fixtures, tile, carpet or skylights

It’s also rarely worth finishing a basement or a garage. But two-tone paint, refinishing hardwood floors, adding tile and upgrading the landscaping are very often worthwhile. Of course, the house needs to be in good shape, and everything needs to be functional. Being a slumlord will hurt you over time. We want to rent solid properties, but luxury items will cost more than the rental value they add. There is plenty of value-add rehab ideas that are great for rentals.

Attention to the front of the house is important. For example, when you compare these photos, the differences are window shutters, clean gutters, a painted front door, and bark mulch landscaping.


In the next two below, the window shutters are strikingly different.


R—Rent (3rd BASE)

Banks rarely want to refinance a property that isn't occupied, so renting usually needs to come first. It's critical to screen applicants diligently so you lease to residents that will pay each month and not damage your property. Good screening is also important for refinancing. While appraisers shouldn't take too much into account about how clean and pleasant the resident is, as noted above, everyone is human and such impressions can make a difference.

When appraising a property currently rented, it is worth requesting an interior appraisal rather than just getting a drive-by appraisal. Appraisers may be more cautious and likely downgrade your property unfairly with a drive-by appraisal. Give your resident plenty of notice via email, letter and reminder phone calls before the appraisal. They don't need to be present but ask them to clean up and kennel any pets if they aren't home.

R—Refinance (HOME PLATE)

The pendulum swings back and forth when it comes to how liberal banks are with their lending policies. They have become less conservative in the last decade. Still, there are things that you need to ask:

1. **Do they offer to cash out or will they only pay off debt?** If they won't offer to cash out, move on and seek out a private loan, or a bank willing to do cash-out refinances, then reinvest private lender funds into the next project.

2. **What seasoning period do they require?** A "seasoning period" is how long you must own a property before the bank will lend on the appraised value versus how much money you have in the property. For the BRRRR strategy to work, you need to *borrow on the appraised value*. Some banks are willing to lend on the appraised value as soon as a property has been rehabbed and rented. These are the ones you want to find which are usually community and regional banks.

The most effective way to find such banks is to ask around. Ask any investors you know which banks they use or go to your local real estate club and ask there. If a bank is lending to another investor, there is a good chance they will lend to you.

We've used another way to find such banks that has been quite effective for us. First, pick a market you are investing in. For example, I would pick Grandview, MO (a suburb of Kansas City). Pick a comfortable loan range (i.e., $60,000-$120,000). Use websites such as ListSource or DataQuick to search for every loan made in that city in your price range during the last year or so to non-owner occupants. This data will likely cost you a couple of hundred dollars but could be well worth it.

Once you have the list, pick out all the banks. Right off the bat, you know the banks that are willing to lend to investors in the area at the price point for which you are looking. They have done it before, so there is a good chance they will do it again.

Finally, make sure to provide the lender with as much information in as clear a way as possible to 1) impress them (remember, these are human beings, not computers making decisions) and 2) help them to decide quickly. The same should go for whatever information, if any, an appraiser requests.

R—Repeat … Rinse and repeat!
If you do the BRRRR strategy right, and run the bases appropriately, you should have a cash-flowing property for little or nothing down. The buy and hold strategy necessitates delayed gratification and many investors attest to the fact that it allowed them to 'survive' until the fantastically profitable I-D-E-A-L dynamics of real estate "kicked in." They will kick in, and BRRRR will see you through until they do.

Now, back to baseball. Let's take a closer look at our sources of financing our deals at the front-end of purchase!

CHAPTER 3
FINANCING ON THE FRONT END

BRRRR: Buy—**R**ehab—**R**ent—**R**efinance—**R**epeat

➢ **HOME PLATE**
—Banks, Seller Financing or Private Lenders and Accounting

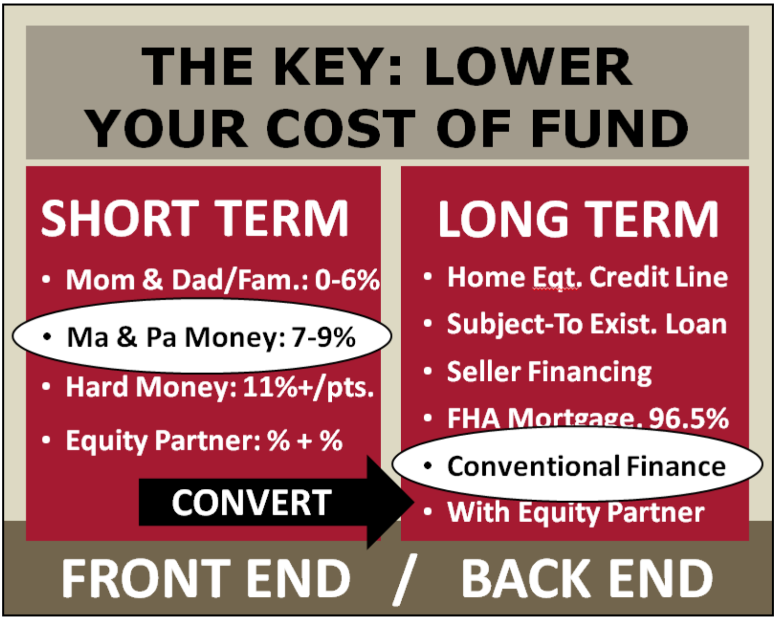
Our Lenders: Money makes the real estate world go around. If the exit strategy is to buy and sell (flip), we need capital for marketing, the purchase, and for rehab. When holding, we may use a bank loan, personal funds or seller financing, and we also have the option of private lending. If so, we will likely finance twice: when we buy (the "B" of BRRRR) using higher interest capital and when they refinance (the third "R" of BRRRR) with longer-term, lower interest bank funds.

When I (Bill) started investing, I had a great advantage because my dad not only loaned me money at low-interest rates, he also co-signed (putting up his name and liability) on loans for which I could not qual-

ify. Later I found a "hard money lender" charging 11% interest, with 2 to 3 points (a point is 1% of a loan). Hard money lenders charge points for their service, higher interest rates and likely have more exacting lending criteria than non-professional, "Ma & Pa" lenders.

But they understand the business well and are easier to borrow money from with unrenovated properties than banks. If the deal is good enough, the expense of their capital may make sense. (If necessary, we also have the option of taking on an equity partner to share profits in a sale or equity in a hold.)

Over time our company began finding our own private lenders at 7-9% interest which I call "Ma & Pa Money." These funds come from non-professionals with $50,000 to $500,000 to lend. Such capital may come from their (self-directed) IRA or 401(k). The second step for holders, after rounding all the bases, is to convert this short-term, higher interest private loan into long-term lower interest bank financing to lower our cost of funds as depicted in the chart below. (And, once refinanced, we find another loan for the private lender.)



Your Competition for Investment Dollars

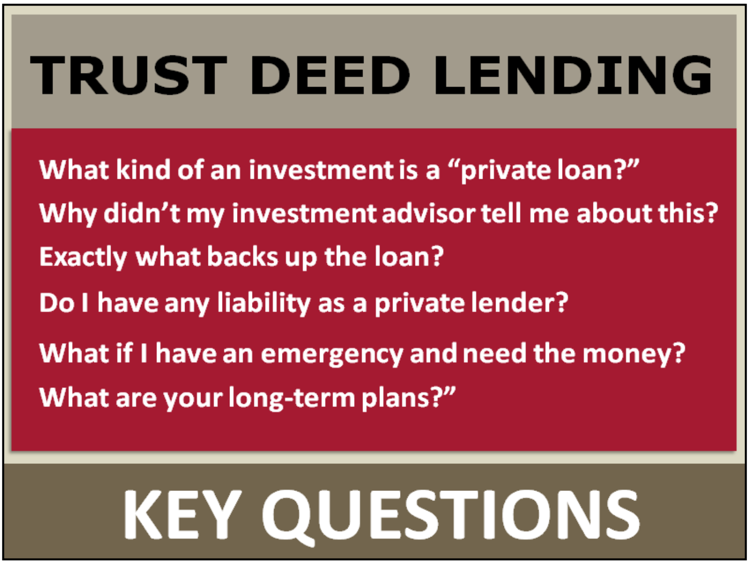
Potential private lenders are everywhere. Studies have shown that 22% of American workers—that's 30 million—have at least $100,000 in their retirement account. What are their investment options? Over the last 100 years the stock market has given investors about a 10% return. Not bad but also not reliable year-to-year. Currenting ten-year treasuries are around 1.75 % and CD rates around 2.25%. If you want to keep your money in the bank, rates drop right through the floor!

Given the alternatives of a vacillating stock market or hibernating in low-interest CDs and saving accounts, many are grateful to find a fixed rate option with a higher rate of return because of the *Rule of 72*. Your interest rate divided by 72 years, results in how long it takes to double your money: 1.5% takes 48 years, 8% takes nine years, 9% takes eight years. For more on info. on private lending to us, visit TheGoodStewards.com.

Balance	Interest Rate
$500-$9,999	0.30% APY*
$10,000-$24,999	0.50% APY*
$25,000-$49,999	0.60% APY*
$50,000-$99,999	0.70% APY*
$100,000+	1.10% APY*

How do you find private lenders?

The challenge is, most potential private lenders have not heard of trust deed (or mortgage) lending because it is not a means through which a financial advisor can get paid. It is up to us to show them the kind of win-win relationship we can develop with them: They get a solid rate secured by a trust deed or mortgage on a piece of cash flowing real estate while we get the capital we need to rehab, rent and eventually find a bank to refinance the property. Depending on a few variables, the interest rate paid to our private lenders is almost always between 7 and 9%, interest-only. Here's some typical questions:



It’s obviously best to connect with potential private lenders *before* needing them. So, we continually add to our potential list as we meet people in social settings, at our local REIA, and through business contacts. We want to tell our story and let our passion for real estate investing shine through.

Remember, we're not begging for money; we're looking for win-win business relationships. One of the primary functions of our websites is to show private lenders what we do and how we do it. The more proactive we can be when we don't need the money, the less it will feel like pleading when we do need it.

Do you have, or can you put together, a "credibility kit" that shows what you do and how you do it? Before and after photos of rehabs you've done create an effective visual image via hard copy and/or a web page. People love to be part of the rehab process, even if as a private lender. They can see that they too are contributing to our communities by giving the housing stock a facelift and cleaning up neighborhoods. Take them on tours with you of your before and after products. Give them ownership of the process and the outcome!

Many potential lenders have their funds in a tax-differed IRA or 401K plans and wonder if there is a way to get their hands on these funds to invest outside of the typical products offered by their financial advisors. It is worth it to get some knowledge and expertise about "self-directed" IRAs and 401Ks that such investors can set up to lend their funds to you and continue to keep their tax differed status. Again, it's a win/win opportunity. Here's a variety of answers to questions about setting up such self-directed plans: http://tinyurl.com/yyawzuge

Stewardship provides its partners with access to capital at the same 7 to 9% interest-only rate with no points we pay our private lenders. Our goal is to have all our front-end financing needs come from "Ma & Pa" lenders—who are pleased with such a return on their money.

Once we have an interested lender, we find out how much they have to lend and match up a property on which to collateralize a loan close to that amount. Then we email them a *lending packet.* This packet highlights that collateral with photos of the property, purchase price, amount and specifics of the rehab, as well as some comparable values like the following one on a house in Indianapolis. (We call our group who oversees our finances and accounting, *Stewardship Capital*.)

STEWARDSHIP PROPERTIES

1843 Singleton, Indianapolis, IN 46203
After Repair Value: $155,000

- Purchase Price: $62,500
- Rehab: $50,000
- Total Cost: $112,500
- Layout 3/1
- 1124 sqft
- Taxes: $1,293

8% interest-only loan; $112,500 loan @ 8% interest = **$750** per month / **$9,000** per year

Scope of Work:

- Remodel Kitchen
- Remodel Bathroom
- Refinish Flooring
- Service HVAC
- Build Deck
- Carpet/Paint

Market Activity/Comps

Our analysis, given the strong neighborhood sold activity, tells us that this house will conservatively be worth $155,000 once our rehab is completed.

Expected Rent: $1,500

St	Type	Address	Area	Price
Act	SFD	334 E Minnesota St	4913	$86,000
Act	SFD	921 E Minnesota St	4913	$94,500
Act	SFD	735 Lincoln St	4913	$110,000
Act	SFD	711 E LINCOLN St	4913	$125,000
Act	SFD	940 E Pleasant Run Parkway No	4913	$129,900
Act	SFD	405 Lincoln St	4913	$169,990
Act	SFD	1836 NEW St	4913	$265,000
Act	SFD	527 Lincoln St	4913	$279,900
Act	SFD	819 Lincoln St	4914	$235,000
Act	SFD	802 E MINNESOTA St	4914	$269,900
Pend	SFD	1814 Orleans St	4913	$85,000
Pend	SFD	349 LINCOLN St	4913	$145,000
S	SFD	909 E Minnesota St	4913	$70,000
S	SFD	719 E Minnesota St	4913	$70,000
S	SFD	917 E MINNESOTA St	4913	$86,000
S	SFD	711 E Minnesota St	4913	$90,000
S	SFD	1841 New St	4913	$95,000
S	SFD	733 E Minnesota St	4913	$228,000
S	SFD	820 E Minnesota St	4913	$238,000
S	SFD	805 E Iowa St	4913	$255,000
S	SFD	519 LINCOLN St	4913	$265,500
S	SFD	620 Lincoln St	4913	$267,000

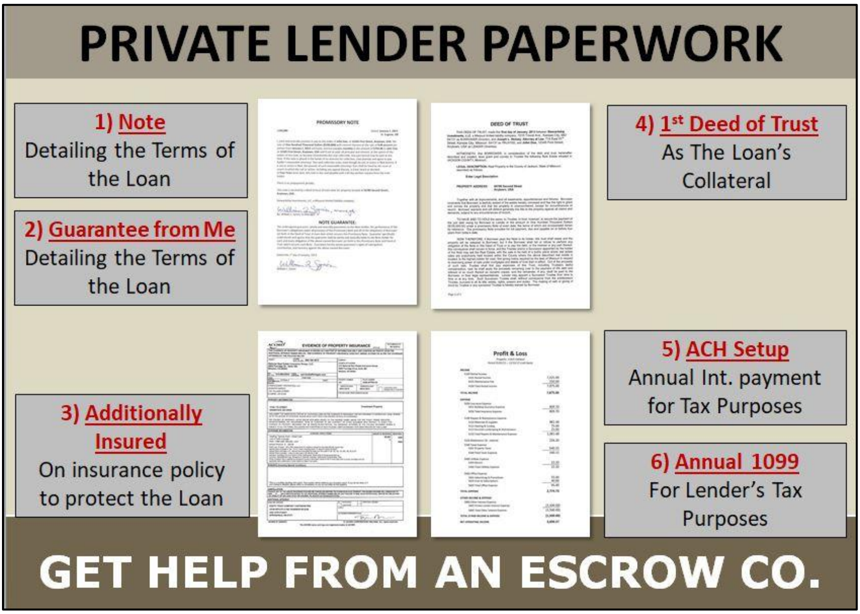
What we like about this Property:

This property is in a trendy area of Indianapolis known as Bates Hendricks. The area is experiencing rapid appreciation and growth as well as new construction. This property has a 4-car heated workshop and garage that will allow us to command a premium rental rate.

When a private lender signs off on the collateral, we then provide:

1) A note with the terms of the loan from the borrowing entity
2) A personal guarantee from me (Bill)
3) A trust deed (or mortgage) recorded in the property's county
4) The lender listed as "additionally insured" with our insurance.
5) A form to set up automatic ACH payment
6) An annual, ongoing year-end 1099 for their tax purposes

Tip: We make our notes for two-year term with a written 30-day call after two years. So, if a lender wants the loan to continue, there is no need to rewrite it. (If asked, however, we pay it back promptly.)



Accounting for Dummies (i.e. many of us real estate investors)
If our business had a least popular list, accounting would likely be near the top. Accounting and entrepreneurship are pretty much polar opposites. But accurate accounting is not a tack-on item for a company's survival. It's a key growth component. Maybe it would make more sense to assign accounting a different, more strategic name. Let's call it: *Cash Management*. And you would do well to know the basics.

The property management/accounting software Stewardship uses is RentManager, which includes a robust accounting module. You don't have to be an expert accountant, but there are two statements that gauge the "financial health" of a property. On the next page is a *"Profit & Loss" statement* which shows a property's net income (in this case a fourplex in Emporia, KS.) Another vital statement is the *"Balance Sheet"* that includes purchase price, rehab costs and capital (long-term) expenditures. It includes the liabilities with the property.

Profit & Loss

Property: 8th, W 216 (SHI-2017)

Date Range: 01/01/17 - 12/31/17 (cash basis)

INCOME	
4100 Rental Income (non-posting)	
4101 Rental Income	15,071.33
4103 Pet Fees	625.00
4108 Application Fees	75.00
4110 Late Fees	74.50
4100 Total Rental Income (non-posting)	15,845.83
TOTAL INCOME	**15,845.83**

TOTAL EXPENSE	**7,514.79**
NOI	**8,331.04**

Profit & Loss 12 Month Recap

Property: 8th, W 216 (SHI-2017)

Monthly recap 01/01/17 - 12/31/17 (cash basis)

	JAN 17	FEB 17	MAR 17	APR 17	MAY 17	JUN 17	JUL 17	AUG 17	SEP 17	OCT 17	NOV 17	DEC 17	TOTAL
INCOME													
4100 Rental Income (non-p	582.66	850.00	855.00	850.00	1,475.50	862.17	1,840.00	1,840.00	1,120.00	1,540.00	1,965.50	2,065.00	15,845.83
TOTAL INCOME	**582.66**	**850.00**	**855.00**	**850.00**	**1,475.50**	**862.17**	**1,840.00**	**1,840.00**	**1,120.00**	**1,540.00**	**1,965.50**	**2,065.00**	**15,845.83**
EXPENSE													
5010 Management Fee Exp	0.00	0.00	0.00	183.01	0.00	0.00	255.01	0.00	0.00	0.00	0.00	0.00	438.02
5050 Insurance Expense (r	132.83	132.83	132.83	132.83	132.83	132.83	132.83	132.83	132.83	132.83	132.83	132.87	1,594.00
5100 Repairs & Maintenan	0.00	195.30	0.00	79.15	120.00	15.19	403.26	215.79	10.85	13.50	95.52	27.00	1,175.56
5300 Taxes Expense (non-	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	1,927.33	1,927.33
5400 Utilities Expense (nor	0.00	113.58	86.50	138.70	118.50	181.56	208.91	257.01	259.30	376.78	194.65	294.39	2,229.88
5650 Bank Fees	0.00	0.00	15.00	15.00	15.00	15.00	15.00	15.00	15.00	15.00	15.00	15.00	150.00
TOTAL EXPENSE	**132.83**	**441.71**	**234.33**	**548.69**	**386.33**	**344.58**	**1,015.01**	**620.63**	**417.98**	**538.11**	**438.00**	**2,396.59**	**7,514.79**
NOI	**449.83**	**408.29**	**620.67**	**301.31**	**1,089.17**	**517.59**	**824.99**	**1,219.37**	**702.02**	**1,001.89**	**1,527.50**	**-331.59**	**8,331.04**
N/O EXPENSE													
6230 Mortgage Interest Exp	0.00	0.00	466.67	466.67	466.67	466.67	466.67	466.67	466.67	466.67	466.67	0.00	4,200.03
TOTAL N/O EXPENSE	**0.00**	**0.00**	**466.67**	**466.67**	**466.67**	**466.67**	**466.67**	**466.67**	**466.67**	**466.67**	**466.67**	**0.00**	**4,200.03**
NET INCOME	**449.83**	**408.29**	**154.00**	**-165.36**	**622.50**	**50.92**	**358.32**	**752.70**	**235.35**	**535.22**	**1,060.83**	**-331.59**	**4,131.01**

Balance Sheet

Property: 8th, W 216 (SHI-2017)

As of 12/31/17 (cash basis)

ASSETS	
Bank	
1090 1090 - Emporia State Federal C U	1,743.49
Total Bank	1,743.49
Other Current Asset	
1200 Undeposited Funds	130.00
Total Other Current Asset	130.00
Fixed Asset	
1499 Investment and Improvement	192,619.46
1510 Intangible Assets	4,076.00
Total Fixed Asset	196,695.46
TOTAL ASSETS	**198,568.95**
LIABILITIES & EQUITY	
Liabilities	
Other Current Liability	
2009 Security Deposits (non-posting)	2,365.00
2900 Prepaid Rent - Unallocated Prepay	80.00
2117 N/P - SPG to SHILLC(Emporia)	121,992.94
Total Other Current Liability	124,437.94
Long Term Liability	
2400 N/P - Private Lender Loans	70,000.00
Total Long Term Liability	70,000.00
Total Liabilities	194,437.94
Equity	
3000 Net Income	4,131.01
Total Equity	4,131.01
TOTAL LIABILITIES & EQUITY	**198,568.95**

Numbers can be brutal things. But having a clear summary of where you are, whether it involves one project or the entire company, frees you to make needed business decisions that are critical to your financial health, including considering ways to increase revenue primarily through rent (from value-add) and lower expenses. Having your books in order is also vital when seeking to borrow or refinance from banks.

The Difference between Capex and Opex

One of the challenges for accounting is to correctly apply longer term capital expenses (capex) and shorter-term operation expenses (opex). For more about the differences: https://tinyurl.com/ya2rqxfj

	Capital Expense (CapEx)	Operating Expense (OpEx)
Purpose	Assets purchased with a useful life beyond the current year	Ongoing costs to run a business
When Paid	Lump sum up front	Monthly or annual recurring
When Accounted For	Over a 3 to 10 year lifespan as the asset depreciates	In the current month or year
Listed As	Property or equipment	Operating cost
Tax Treatment	Deducted over time as asset depreciates	Deducted in the current tax year
Example	Buying a laser printer	Buying toner for printer

Capital expenditures are for major purchases that will be used for many years, or at least beyond the current accounting period. They go on the balance sheet because such expenses are recovered over time through depreciation, Capex expenses further the overall capability of your business so they are separate from the operations budget.

Operation expenses are the day-to-day expenditures to keep the business running. These are more short-term costs used up in the same account period they are purchased (and tax deductible in that year).

Both expenses directly affect your bottom-line profit, but they should be treated differently. If you purchase a truck, it’s obviously a long-term capital expense but its change of oil, replacement of the water pump, or other such expenses are necessary to keep it in operation.

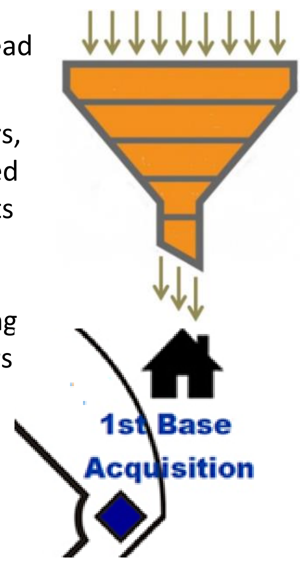
So it is with property. Replacing a roof, HVAC or water heater are long-term capex expenses. But they still cost you money today and reduce your profitability. *The problem becomes how you keep your buy/hold business profitable in the face of such expenses.* If your property portfolio is growing in value (through equity build up and increased rents, then these value increases should help pay for capex over time.

CHAPTER 4
ACQUISITON, PART 1: FINDING THE DEAL

BRRRR: Buy—**R**ehab—**R**ent—**R**efinance—**R**epeat

➢ **1st BASE**
—Acquisition

If we have a real estate mantra, it's this: *you must begin with a good, if not great, deal*. There is just no substitute for finding and negotiating a great deal. So how do you do this? In a nutshell, you must look at a lot of potential deals. If you're only getting a few coming your way, widen your funnel. A wide funnel gets them coming to you from many sources rather than forcing you to chase deals and end up overpaying.



Here's where much of your deal flow from lead generation will come from:

- Direct marketing to distressed owners, property managers, foreclosures, tired landlords, bankruptcy, tax deferments (We'll cover this in-depth.)
- Driving for dollars
  Cold calling/texting and live answering
- Website presence/For Sale by Owners
- Word of mouth
- Business cards freely passed around
- Investment-minded agents
- Buying from wholesalers
- MLS hunting

Again, there is no substitute for finding good, if not great, deals. Everything—a good margin for adequate rehab cost, being able to readily find financing, making a profit or positive cash flow and building a stable foundation to pursue larger opportunities—starts with buying properties at wholesale, below market prices. Otherwise, we subject ourselves to an exhausting uphill climb that can leave us wondering why we got into this business in the first place.

What's a Deal, a Good Deal, a Great Deal?

While the public may be fine with the real estate equivalent of convenience shopping at 7-Eleven, we operate like Costco, becoming wholesale-type purchasers ourselves. We cannot buy conveniently at retail; we need a wholesale profit edge. We're "good deal junkies," because the adage is true: *you make your money when you buy*.

So, what is a very good/great deal? Again, as holders our goal is 75% *After Repair Value* (ARV): Purchase Price = 75% ARV – Cost of Rehab.

--At Market: 100% of value: 70 in a 100--70% of all transactions
--An Okay Deal: 90% of value: 20 in a 100--20% of all transactions
--A Good Deal: 80% of value: 9 out of 100--9% of all transactions
BRRRR Deal Target:
--A Very Good Deal: 75% of value in order to refinance out your cash
--A Great Deal: 70% of value: 1 out of a 100--1% of all transactions
(Note: These ratios are guesses, but you get the idea!)

The question:
How do you generate leads to find the best, lucrative deals?
The answer:
Direct-to-seller marketing brings you off-market deals.

Direct to seller marketing gives us an edge in at least five ways:

1) Finding motivated sellers who are prompted to sell for reasons other than getting "top dollar" for their property: Those who want cash now, are recently divorced, behind on payments, facing foreclosure, don't like dealing with Realtors or the public, tired landlords. These "don't-wanters" often bring complications with them but may very well be willing to sell at a Costco price rather than a 7-Eleven one.

Another source of deals comes from affluent homeowners who just want an easy exit and are willing to exchange price for ease. Direct marketing has sellers reaching out to us, relieving us of most of the competition from other investors. It also gives us the benefit of building rapport and finding out about seller's needs without having an agent in the middle of the deal hindering such communication.

2) Focusing on off-market deals. If you're buying before the general public knows about a listing (whether you found it or a wholesaler or agent brings it to you) you are more likely to get a good deal because the seller doesn't want to deal with listing it on the MLS. Granted, there can be competition to get off-market properties, but this is a place to invest your time, energy and money. If you're not getting good deals, you're going to end up with a mediocre portfolio.

A word about "investment-minded" agents. Agents are invaluable if you find the right one(s) who fully understand our purchasing criteria and work hard to find sellers/deals for us. They will need to be comfortable (as will we) with making lots of relatively low offers. We are repeat buyers, but picky ones who cannot settle for what the general public settles for in price or terms. These agents are pure gold to us!

3) Providing opportunities for creative deal-making. Wholesale buyers do not get emotionally attached to properties that we *must have*. We can walk away because we are attached to the number that we *must get*. But as "transaction specialists" we are constantly in training to make something out of nothing with creative deal-making.

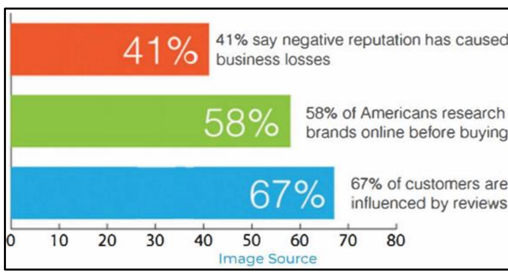
4) Obtaining owner financing where sellers provide nearly all the financing. Cash is king, and we want to hold on to our cash for more deals. Seller financing can allow us to initially avoid financing charges like appraisals and lender fees, giving us the flexibility to rehab the property and then refinance with lower interest bank loans. Getting the seller (or private lender) to take a 2nd position loan to cover the down payment and/or rehab cost allows you to still get a 1st position loan from a bank and be all-in to a property for nothing down.

5) Securing value-add deals where rehabbing, changing usage, adding rental value can increase the value of the property beyond what it costs to make those changes. Sometimes this is called "the wedge," the gap between what a property is worth and what you buy it for. We are problem solvers because it is those very problems that bring the opportunity for building solid equity and profit into our deals.

Finding Discounted Properties from Direct-to-Seller Marketing

Many of us started (or started and stopped or started and continue) yellow postcard or yellow letter campaigns to find motivated sellers. Why yellow? Because yellow stands out. And why postcards? Because postcards are cheap. Or maybe we made an upgrade to yellow letters. They're about 1.25 a pop.

When it comes to direct mail most of our competitors are doing things the exact same way as everyone else and wondering why they're not getting different results. The truth of the matter is you're never going to get extraordinary results with ordinary methods.



If Amazon, Google and Yelp reviews have taught us anything, it's that today's consumers are absolutely obsessed with understanding what sort of experience they're going to get before they pay for it. What I (Ryan) mean is that we're all guilty of looking up reviews and letting other's experiences dictate where we spend our money. I'm as guilty as anyone when it comes to this. Shoot, I've even had a great meal, later read the reviews, and realized ways they could have done better.

The people you're hoping will sell you their house at a steep discount are no different. They tend to fall into two categories:

1st List Type: Eviction, Probate, Divorce, Pre-Foreclosure, Back Taxes
You're either trying to convince a stranger with a distressed property who's often in emotional, social or financial distress and feels like the world is out to get them, that they should sell you what they're told is their largest asset.

2nd List Type: Seniors with equity & Retiring Landlords
Or you're dealing with an affluent individual who is willing to trade equity for an easy transaction.

Chances are both of these groups are much more likely to call a local BBB-accredited, 5-star reviewed home buyer with an easily found website and testimonials over “John Doe Buys Houses."

We would even argue that building a local community brand with reviews, social proof, and a verifiable track record can make the difference between success and failure for investors. Before jumping into things, why not take some time spent building your brand? It can pay dividends for years.

Quite frankly, the data has taught us that building a local community brand is where it’s at. You need a website, you need a Facebook business page that you update, you need a Linkedin page, and your marketing must tie into your brand. Figure that people will google your name and/or your company. If they do, what would they find?

Yellow letters from John Doe, postcards with doodle marks and fake coffee stains do not get results—or, if they do, those results are only a small margin for which your business is capable.

We’re 100% Against Dishonest Marketing.
What does this mean? There is a trend to use marketing that tricks or scares people into calling. Likewise, there is another trend to lie about your intentions.

Image Source

People end up buying from/selling to who they like. How can you build a real relationship if you're starting out with a lie? What kind of legit company would do that?

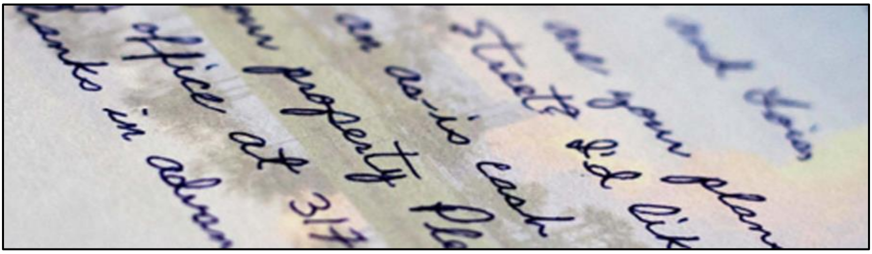
Always pick up your calls from your marketing or hire a live answering service like CallPorter.com. Don't spend thousands of dollars on marketing only to fumble in the end-zone.

So, use the golden rule: Treat people how you want to be treated. Would you rather get a polite letter asking you to call if you're interested or a deceptive yellow letter? Would you rather be able to talk to a real person in the U. S. or listen to some guy you don't know talk about himself on a recording?

Example of this above: 3rd notice postcards, letters that look like a bill, my wife and I are looking to move (when you're not), I can only buy one house this month…. You get the drill!

So, what are we sending now? Check out the following hand-written letter from BallPointmarketing.com

All of Ball Point's direct mail are custom designed for each market, featuring full color local imagery on the front, and a matching pattern on the back, with a full color watermark on the letter.



These pieces aren't printed on a LaserJet, either. They're written in cursive by robot arms. To stand out from the crowd, all these letters are written in beautiful blue ballpoint ink that smears, smudges, digs into the page, runs thinks, runs thin, but most of all, looks quite real. Competitor's printers don't stand a chance!

None of your competition is likely anywhere close to this level of marketing. When you get your mail today, look at it and look at these pictures. Then ask yourself, would this stand out amongst your mass of bills, coupons, postcards, and plain envelopes?

But does it get better results?
That's the question I (Ryan) set out to answer once and for all. During 2018, we ran a massive $250,000 case study in sunny southern Florida. The test was simple. We'd spend $125,000 on typical post cards and $125,000 on Ballpoint marketing mailers.

The results?
--Cost Per Acquisition on Post Cards: $7,000
--Cost Per Acquisition on Ballpoint Marketing: $3,000
In other words, the hand-written (robot-written, really) letters saved $4,000 per deal. The largest franchise (We Buy Ugly Houses) needs to send about 3-4X that many mailers to get a single deal. Think about it!

So, Who Should You Be Sending Your Marketing?
Absentee owners with equity are probably the most commonly targeted list. The reason for this is economies of scale. It's an easy list to get and quite frankly it still works. We average a property purchased for every 1,500 letters when we're mailing to absentee owners. It's

amazing what unique marketing backed by a solid brand can accomplish if…you include a lot of follow-up and hustle!

Divorce, probate, pre-foreclosure, eviction, and code enforcement. The reward with these harder to get lists lies in the fact that your competition is lazy. You're going to have to call your county, you may have to go in person, or even have to file Freedom of Information act requests to get access. But trust me, the juice is worth the squeeze!

Some other ninja options include:
• Houses with no utilities on
• People who are behind on their taxes
• People with bad credit
• People with balloon payments coming due or high interest rates

Driving for Dollars (which is just basically driving around and writing down the addresses of ugly, unkept houses with differed maintenance). Here's a shout out to an app that will certainly streamline this process for you: DealMachine.com.

Two of our other favorites are unknown equity and unknown sale date. Here's how you can pull those:

--How To Pull an *Unknown Equity List* from List Source:
youtube.com/watch?v=2G2JtM237hU&feature=youtu.be

--How To Pull an *Unknown Sale Date Niche List* for Motivated Sellers:
youtube.com/watch?v=ROMncpM7iks&feature=youtu.be

And Don't forget about Mailing Small Multi Owners
We also target 1 to 49 units. One useful data product to collect owner names, addresses and phone numbers is Renomy. For more information: reonomy.com/blog/post/how-to-find-multifamily-properties

Common Direct Mail Conversion-Killing Mistakes
Of course, direct mail isn't just a matter of sending mail and watching people give you money. Here's some rookie mistakes to avoid:

1) Not Having a Local Postmark

We're big fans of having your mail shipped to you locally so you can it's postmarked from your city. If your mail is sent for you from a city you are not living in, it will lead to questions: "I see you've got an X address, but your mail is being sent from a Y address. What's the deal?" Your answer: "I have people who help me: friends, family and associates who help me out with my mail…are you interested in selling?"

2) Not Answering Your Calls and QUICKLY Responding

We did a test in 2017 where we used local numbers and cold called over 600 "We Buy Houses" type companies nationwide. Less than 3% picked up the phone and only one called us back. If you're looking to increase your wholesale/flip volume, or buy more rentals, you've got to treat this like a business. If a seller wants to sell and you don't pick up what do you think they're going to do…often within five seconds!? They're going to call your competition instead.

3) Prejudging your leads

As humans, we all carry certain biases that affect every area of our lives. Signs that you're shooting yourself in the foot include, but are not limited to, 1) thinking a lead didn't sound motivated, 2) assuming they'll want top dollar, 3) taking their asking price at face value, etc. Here's a quote from an unknown source that might help here:

DON'T FORGET: *The seller's asking price is ultimately meaningless. It's not usually based off comparable sales, market research, or fact. Nine times out of ten it's a number they pulled out of thin air."*

Some of our best deals have come from sellers whose asking prices were totally nuts. Why? No one else is giving them the time of day. By meeting with them, building rapport, educating them, and giving them options, you've got a real shot at getting the deal.

Our rule of thumb is that if they have equity and want to sell, you should meet with them. The only time you have earned the right to be picky is when you have more rentals, cash, and leads than you know what to do with. (Note: Please contact us if this is a problem for you. We would be ready, willing and able to start partnering with you!)

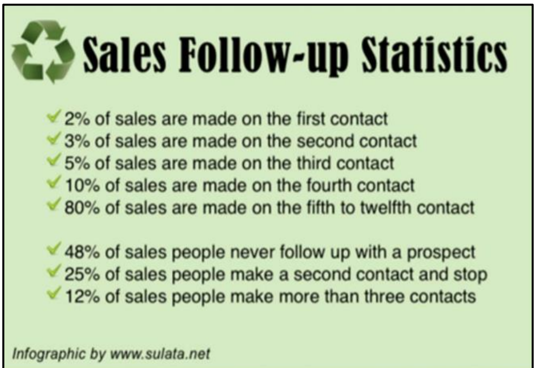


Image Source

4) Not Following Up
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4) Not Following Up

Yes, I meant to do that!
In 2016 I did five-off market transactions. In 2017 I did 74! Why? It all has to do with following up. On one of our deals we figured it out took us 59 touches--follow up calls, emails, texts, thank you baskets, notes, you name it (until we're told to "get lost!")—to secure a great deal. One of our partner's acquisition manager has us beat, though. On one of his deal they counted 65 touches to secure it. This is the kind of commitment that will make you rich! And the lack of such follow-up will do the opposite: keep you poor!

Read about an example of 18 Touches: https://tinyurl.com/yyuc386t

5) Not Being Consistent
Marketing is like playing poker. Some play recreationally and lose. Others see the game as one of odds. They memorize the odds as best they can, learn how to read people, and take their emotions out of it. They have a plan; they use tactics and they have a consistent strategy. They would be offended to be called gamblers!

Likewise, you don't want to be a marketing gambler with no real consistent strategy. Otherwise you end up on the deal hamster wheel, send out mail, get leads, get a deal done…now restart phases one to three. Instead you want to put your marketing on autopilot and send it out every week. Until proven otherwise, and we don't think that will be the case, leave your emotions out of it. Emotions like:

What if it doesn't work for me and I'm the outlier?
My market is probably too competitive, and the good deals are gone.
Maybe I'll just wait for the next crash.

6) Not Using a CRM

A CRM is a Customer Relationship Management system and yes, having one is vital to keep track of your leads and to schedule automatic follow-up sequences. You just can't keep all the balls (deals) in the air and expect many of them to land in the profitable column. The CRM we use is Polio. It's free to a certain point and, when you have to start paying for it, but it's worth every cent: Podio.com

Widening Your Funnel with More Lead Generation Strategies

Guerrilla Marketing

Guerrilla Marketing is a concept coined in 1984 by Jay Conrad Levison in his book *Guerrilla Marketing: Secret for Making Big Profits from Your Small Business.* This kind of marketing aims for maximum exposure through unconventional, innovative and lower-cost exposure. See 122 examples: https://tinyurl.com/2bnv8fz

In the past we've used such things as billboards and even a house truck to get the message out that: *We Buy Houses.* And, however you do it, this is your primary message: *We Buy Houses.* We continue to put this message on the back/sides of our work trucks.

Classified Newspaper and Nickel Ads

In the "good ole days" I (Bill) used the following classified to bring in some tremendous leads, particularly targeted toward value-add properties around the University of Oregon in Eugene:

SAVE THE COMMISSION
Wanted: House or investment property
near campus. Call: Bill at 541-XXX-XXXX

With the onset of the internet, such advertising has largely gone the way of the Dodo bird. However now, given that most people no longer use the classifieds or deem them of value, you could consider them a potential form of lower cost guerrilla marketing!

“Gray Area” Marketing

I (Bill) call these this gray area marketing because, well, what follows falls into a gray area. So, consider this a disclaimer: You should consult with an attorney regarding the legalities of these forms of marketing. Why? Because they hug the line between legal and illegal and it’s possible to be fined or sued. So, proceed with caution.

Bandit Signs
An easy example of this is the use of “Why Buy Houses” type of bandit signs. The problem: Not only do they clutter neighborhoods; they are illegal in many cities. Now, what does “illegal” mean? Okay, yes, we’ve entered a gray area here. You will not get thrown into jail for putting up bandit signs, but you could face a reprimand or be fined, (I’ve heard as much as $75 per sign), because, well, those city compliance officers know who to call!

As a result of their questionable legitimacy, some investors put them up on Friday afternoon and take them down on Sunday night. I must admit to using bandit signs early on in my real estate career, however, I’m not sure I got any deals from their use. What I would suggest is putting up signs in front of houses you’re rehabbing and on your vehicles. For more see: fitsmallbusiness.com/bandit-signs

Ringless Voicemails
RVM allows you to drop voicemail messages directly into a recipient’s voicemail box without their phone ringing but leaving a notification, “you have a new voicemail.” It’s a kind of backdoor method to get out your message without disrupting the recipient in the way a regular phone call would.

While you can reach many would-be sellers in scale, these calls are considered intrusive and spammy. In 1991, Congress passed the TCPA. The law is meant to protect consumers from any calls using automated dialers, faxes or SMS messages. The FCC regulations impose financial penalties on all commercial telemarketers for calling phone numbers on the “Do-Not-Call” registry.

The key component of the TCPA is the amount of damages available for violations. Damages range from $500 to $1,500 (if willful or knowing) *per call* with no cap on aggregate damages. There are a number of people who make a living seeking to caught TCPA violators and many of them end up on the litigator’s list: litigationscrub.com

Companies that use ringless voicemail make the claim that this law does not apply to them since there is no actual “ring” or call made. Real estate investors further point out that they are not soliciting a sale but, instead, seeking to buy (a house). In response, the FCC, consumer advocates and lawsuits across several states (including an explicit law in Florida law starting July 1, 2018) have said otherwise.

This has led to some using what are called “voicemail drops” which require an actual person to make a call and then, when the phone goes unanswered, they leave a prerecorded voicemail. Advocates of voicedrops point out that this is a legal form of communication because it does not include an automatic dialer. But, of course, the fact that there is a person involved increases the costs substantially.

There are several companies that facility uses of these technologies, including one that many investors use called Roar.com. Again, you would be wise to tread lightly and know the litigation downside. For more information: paceregulatoryguide.com/landing-pace/TCPA

Text Messaging

Text messages also come under the same consumer protections of TCPA and should be considered accordingly. Those investors who use text blasting secure multiple, even hundreds of phone numbers because the phone carriers only allow about 25 texts to go out per day per phone before blocking them. They identify themselves as a local investor interested the potential purchase of the recipient's property and leaves a phone number for them to call back if interested.

Cold Calling

Many investors also use VA's (virtual assistants) to call homeowners directly. It is possible to use out of country VA's, like those from the Philippines, to call scrubbed list of owners with equity or out-of-state landlords. They can make as many as 500 calls a day to such a list. Calls to distressed homeowners, like those in behind in payments, recently divorced, in probate, tax deferral status, etc. are often called by callers who require a higher level of communication skills, so in-country call centers are usually more successful in handling such calls. Relevant lists can be obtained from companies such as SkipGenie.com.

"White Area" Marketing

Google AdWords

If you've done a google search, you've seen google adwords which are paid advertisements placed above the organic search terms. Google targets niche audiences by putting into their search criteria a specific location. So, if you're looking to purchase properties in Tampa, Florida you can target those zip codes accordingly.

There are companies that focus solely on overseeing Google Adwords for clients. GeoFlip.com does this for real estate investors, charging a flat $1,500 monthly fee while suggesting a minimum of a $3,000 monthly add purchase. Their service includes a weekly "Golden Ratio Call" where they evaluate the leads/deals with their clients versus dollars spent.

What follows are the highest 63 "keywords" for those who look to Google searches in order to sell their house. Also, there are another 1500+ keywords to avoid using in order to not spend money unnecessarily on searches that don't lead motivated sellers to you.

The 63 most search terms fall into four categories: 1) buy fast, 2) cash for house, 3) buy quickly, 4) sell for cash, 5) ugly houses, 6) sell quickly, 7) fast for cash, 8) buy house, 9) house investors and 10) buy fast.

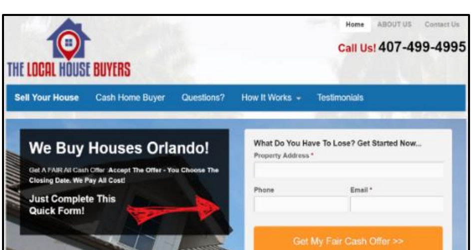
"buy my house fast
"we buy houses fast"
"house buy fast"
[who can buy my house fast]
"buy your house fast"
"quick cash for homes"
"cash for your house"
[cash for your house]
"quick cash for houses"|
"cash offer for my home"
+cash +home +offer
"cash home offer"
[get cash offer on house]
[receive cash offer for home]
[we buy houses quickly]
"we buy houses quickly"
"sell house cash"
"sell my house for cash"
[sell your home for cash]
[sale my house for cash]
"sale my house for cash"

"how to sell your house for cash"
[i buy ugly houses]
[ugly houses]
[sell ugly house]
[quick sale home]
"quick home sales"
"how to sell a house quickly"
"how can i sell my house quickly"
[i need to sell my house quickly]
"i want to sell my house quickly"
"quick sale your home"
"how to do a quick sale on your house"
"quickest way to sell a home"
"homes for quick sale"
"the best way to sell a house quickly"
"sell your home quickly for cash"
"sell my house quick for cash"
"fast cash home offers"
"fastcash4homes"
[fastcash4homes]
[real estate buyer]

"how to sell your house for cash"
[i buy ugly houses]
[ugly houses]
[sell ugly house]
[quick sale home]
"quick home sales"
"how to sell a house quickly"
"how can i sell my house quickly"
[i need to sell my house quickly]
"i want to sell my house quickly"
"quick sale your home"
"how to do a quick sale on your house"
"quickest way to sell a home"
"homes for quick sale"
"the best way to sell a house quickly"
"sell your home quickly for cash"
"sell my house quick for cash"
"fast cash home offers"
"fastcash4homes"
[fastcash4homes]
[real estate buyer]

Facebook Ads
Paid facebook ads get seller attention and leads, as does **Instagram** use. Here's the face-book page that Brandyn Schwalm uses for N. FL: facebook.com/thelocalhousebuyers

For more info. on putting together a strategy to place ads wisely: socialmediaexaminer.com/facebook-ads-ultimate-guide-businesses



Website Presence (and SEO)
You will have to spend a lot to get into a 1st position on an organic "we buy houses" search. But a basic website will introduce you and what you do. Check out: carrot.com

Qualities of a Great Acquisition Manager

They know how to build rapport
A natural acquisition person is a natural rapport builder. They like people and people like them which is critical because people want to do business with people they trust, like and feel comfortable with.

They don't come across as salespeople
Good acquisition people are comfortable in their own skin and are genuinely themselves. They are friendly and empathic with the seller.

They are good at sizing up situations
When a good acquisition person walks into a property, they quickly size up the sellers, their situation and "the deal" they are in. They consider cost and potential as well as what's important to the seller.

They are hard to discourage
Digging deep is what great acquisition people do. The word "no" is not going to stop them from finding a way to build a bridge to the seller and to find a way to a mutual beneficial solution. They will follow up until their last breath or until they hear, "Stop Contacting Me!"

They are ambitious and organized
Setting goals, working through them step-by-step, effectively using low cost VA's—Virtual Assistants (especially with data), then celebrating achievement, comes naturally to great acquisition people. They are energized to better themselves in the service of others.

Buying a Portfolio of Properties: 9, 17, 32, 41 and 97

Buying groups of properties all at once is a great way to rapidly increase the size of your portfolio. The key, of course, is being able to find, evaluate, and finance such deals. I've describe our purchase of various property portfolios in BiggerPocket articles, including 17 condos, 41 and 97 houses and a 32-unit apartment complex. Here I (Andrew) will discuss a more reasonably sized package of nine houses we bought and what we learned from it.

Finding the Deal

This deal came to us in a very simple manner; a wholesaler emailed it to me. Now, most of the properties I see from wholesalers range from OK to terrible. The portfolios are usually particularly bad, with most of the properties residing in the absolute worst parts of town.

Part of the reason for this is that wholesalers will often develop strong relationships with a couple of end-buyers, and those investors will get to pick over their deals first. So, all the good ones get gobbled up, and the one's that get to you are usually mediocre at best. On that note, it's a good idea to find the best wholesalers and try to become one of their go-to investors. Take the best one's out to lunch, and if you do buy a deal from one, try to leverage that into another.

But even though most of the quality purchases will get snatched up before they land in your inbox, some of the good ones will slip through the cracks. I've purchased plenty of properties from wholesalers by simply being on their email lists.

While you'll have to sift through a lot of coal to find a diamond and learn to ignore heavy-handed sales language like "Cash Cow," or "25 percent cash on cash return," or "this property will cure cancer," it's still worth the effort. After all, all you have to do is get on an email list and check to see if the property and price look reasonable. Most wholesalers will include a lot of pictures, so that can help you do a quick evaluation as well.

Move Quickly

When you get an email from a wholesaler with an interesting property, you can bet that a bunch of other people got the same email. In the past for example, when a wholesaler sent me a house that would have been a great deal, I got there right as another investor was leaving. As soon as I had finished walking through the house I called and let the wholesaler know I would take it. Unfortunately, the other investor had already locked it up. That's how fast this game can move. So, try to get in the property as soon as possible!

On this package of nine, I called the same day and set up an appointment for the following day. This was the soonest we could get in. In the past, I have made a couple of blind offers on properties I knew I wanted. But oftentimes sellers will be hesitant with those because they (rightfully) think there is a high chance you'll back out upon seeing the property. It also makes you seem desperate. You don't want to be a motivated buyer any more than a motivated seller. Occasionally, blind offers may be appropriate. But I haven't generally found them to be useful.

Talk to the Seller

I've found that with wholesalers, it's usually easier to talk to the actual seller than it is when the property is listed with a real estate agent. On a run-of-the-mill deal, that might not be necessary. But on one that may require terms such as seller-financing, or on a larger deal like this one, it is always a good idea to meet with the seller. Never underestimate the importance of building rapport!

On this occasion, we were able to meet with the seller at the one vacant property in the portfolio. We built rapport while getting as much information from the horse's mouth about the properties themselves. This is always a critical step. The seller needs to trust you and want to sell the properties to you. By building this trust, you can increase your odds of stemming off any other last-minute suitors.

Valuing the Deal

A lot of big investment firms that buy houses such as American Home Buyers, B2R or Colony Homes value large portfolios of houses in the same way normal investors value apartments; by looking at their cap rate and gross yield (annual rent divided by total cost). Unless you own or work for such a firm, I wouldn't recommend this.

Yes, you need to analyze deals to see if they will cash flow. But more importantly, you should value these properties based on their ARV. We want our portfolios to meet the same ARV requirements that our individual purchases do. For these, it took a little while to put together nine comparative analyses (albeit a lot less time than when I put together 97), but it is an important step. You never want to just shoot from the hip, especially when buying multiple houses at once.

We were only able to walk through two houses beforehand. The other seven I drove by. So, I listed out my assumptions on our offer. I said that I expected that all nine were habitable and that, while would be some deferred maintenance, but that there were no major required renovations. What it does, especially on larger offers, is gives you something to point to if you find a bunch of problems that weren't disclosed prior to going under contract. If need be, this makes it easier to retrade with the seller. They didn't meet agreed upon expectations.

Due Diligence and Closing

Allow me to stress something here: walk every unit! Sometimes, you may not be able to; for example, one of the major points during our negotiation on the 97-property purchase was that the seller didn't want to go through all 97 of them. But we felt the price and terms justified that *as long as* we made a major contingency in our analysis that we were taking on some of these properties relatively blind. Whenever possible, walk each unit.

On this deal, the seller agreed to let us walk each one and luckily the properties were more or less as expected. We weren't able to get much in the way of an operating statement. But again, we felt the price justified that *as long as* we made a contingency in our analysis for that unknown.

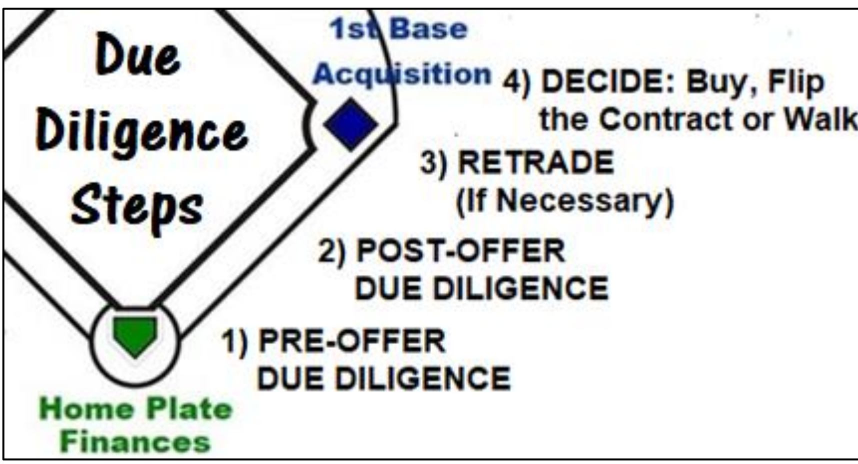
For the financing, we used the same technique we used to close our 41 properties. We set the close date to be shortly after a bank refinance on a portfolio of houses we already owned and had private lenders on. Then we simply asked those private lenders to lend on the new properties. Given these lenders wanted to keep receiving their interest payments, they all said yes. This method calls for a lot of paperwork, but it's a great tool to add to your BRRRR strategy, particularly with regards to buying small portfolios of houses.

CHAPTER 5
ACQUISITON, PART 2: EVALUATING THE DEAL

BRRRR: Buy—**R**ehab—**R**ent—**R**efinance—**R**epeat

➢ **1st BASE**
—Acquisition

The first time you lay eyes on a property you've begun the due diligence process. It starts in earnest once you've gotten the property under contract. The "due diligence period" is when you, as the buyer, do your homework (inspections, securing financing, title work, survey) in order to make your final purchase decision of "yes," "no," or "I need further concessions." It can be divided up into the four steps below:



"Confirmation bias" is our tendency to interpret new information based on preexisting beliefs. Our first impression of a deal/property may very well color, either positively or negatively, the facts of that deal, filtering out issues we are predisposed to include or not include in our further analysis.

A process of strict due diligence can help us to fight against this tendency, not to mention the agenda of a seller or an agent. Our "gut instinct" is served best by collecting all the pros and cons we can.

For a more detailed treatment of due diligence, especially when applied to buying multi-family, see Andrew's Due-Diligence-Guide.

Estimating Rehab Costs

There are a lot of things to look for when doing your initial (as well as post-contract) walkthrough. The first thing is to simply get a good feel for the property. Would you grade it as being close to rent ready or bulldozer bait? Maybe somewhere in between? You should always note a property's general condition.

More specifically, the following items should be on your radar:

Furnace and A/C: Are they old or rusty? Evaluate them as well as possible. Fuse boxes really need to be replaced with an electric panel.

Electrical Panel: Make sure it's in working order, at least 100 amps (unless it's in a small apartment), and not a Federal Pacific or Pushmatic panel, both of which you should probably replace.

Ungrounded Electrical Outlets: You can use a plug tester from Home Depot or Lowe's to test for this.

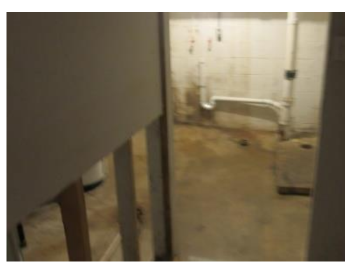
Plumbing Leaks: Run the water, check each of the faucets, and look in the basement (if accessible).

Galvanized Plumbing: Lookout for steel pipes, which tend to rust and is the cause of low water pressure. These will likely need replacement.

Foundation Cracks: These could be signs of bad grading or roots pushing on the wall and should be epoxied and likely shored up with braces. (Note that horizonal cracks are much worse than vertical ones.)

Foundation Movement: Anything over four inches should probably be braced or have "dead men" added. Much more than that and the wall might need to be pushed back, which is very expensive. (Pro tip: If you can't tell how much the wall has moved, go outside and run you finger along the bottom of the siding. It should go about to your knuckle. But just running it along the foundation wall should give you an idea of where and how much the wall has moved.)

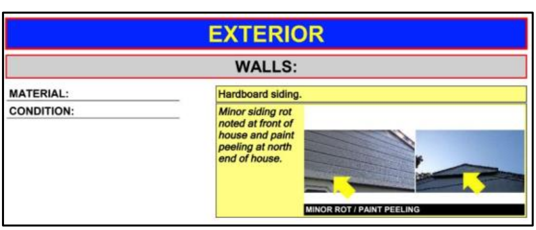
Mold: This usually occurs in the basement. Also look for the bottom half of the drywall missing (like in the second picture below). This virtually always means mold was torn out. Mold isn't hard to remove, but the key is to find out where water is getting in so new mold doesn't grow back. This could be easy or very difficult, depending on the house.



Roof Leaks or Damage: It will be hard to tell if the roof leaks unless it's raining, but you can see damage by getting on the roof. How many layers are there? More than one is a problem. Check from a side view, too. If the edges of shingles are lipping up, that means the roof's old and on borrowed time. If you see what look like small, discolored impact craters on it and granules are missing, that’s probably hail damage.

Sewer: Get the sewer line scoped on any property over 30 years old. Replacing a sewer line can be an expensive proposition (usually over $5,000), so you want to find out whether the line has collapsed or is ridden with roots.

You should be able to get a plumber to scope it for around $200. Make sure to view it with them so you can evaluate if roots can be snaked out rather than needing replacement.


EXTERIOR

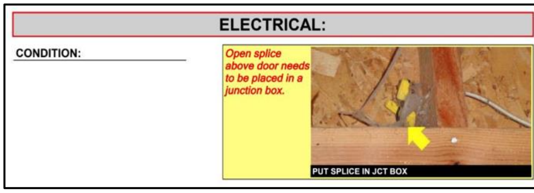
WALLS:

MATERIAL:	Hardboard siding.
CONDITION:	Minor siding rot noted at front of house and paint peeling at north end of house.

MINOR ROT / PAINT PEELING

If you’re just starting out (or even seasoned) it would be wise to get an inspection from a pro. They can be a bore to read but do so anyway!

Some issues, like the above, are rather small. Others, like the one below, definitely need to be addressed and maybe before purchased.



You shouldn't rely entirely on an inspector either. Thoroughly walk through the property yourself, as well. But inspectors can certainly catch things you missed and will generally know a lot more about building and safety requirements than you.

Furthermore, inspections can be used to verify your rehab expectations, realize you need to look deeper into something, or be used for retrading. Many buyers demand a seller fix all or some of the problems an inspection brings to light before they are willing to close.

Additional inspections you may want to consider, include:

Lead, Asbestos and Radon Inspections

Termite Inspection: Especially if you see signs of damage like the joints in this photo or from mud tunnels below.

Roof Inspection: If the roof is older, appears damaged, or you are not sure about it.

Phase One: Environmental inspection for commercial.

Alta Survey usually used for unclear easements, etc.

Unsure of something? Ask a specialist. For example, you could ask an HVAC technician to look at the furnace in a property if you're not sure of its condition. Either way, you want to know what you're dealing with ahead of time. You're certainly not going to win the adoration of any renters if they have raw sewage back up into their home!

When Is Retrading Necessary…or Just Desirable?

There are two major reasons for due diligence. The first is to make sure the property is what you thought it was. The second is to give you the chance to renegotiate if it's not. With due diligence, real estate is not only safer but also more profitable.

For larger deals, I (Andrew) like to list my assumptions up front. Examples of assumptions might be that approximately 90% of renters are paying, the HVAC is in pretty good working order, the roof needs to be replaced, and so on.

By documenting this, if assumptions are proven inaccurate when performing due diligence, they can be referenced when asking for a price reduction. But even without such a list, you can always ask for a price reduction or amend other terms if you find something amiss. Remember, everything is negotiable.

Aside from a price discount, problems discovered during due diligence might be resolved by asking for certain issues to be fixed, asking for financing, asking to extend the closing or inspection period, or some other way.

That being said, you shouldn't plan on retrading from the get-go or retrade over something trivial. If you do, you'll quickly get a reputation and sellers will be less likely to want to do business with you.

Final Decision and When to Walk Away
When all the hay is in the barn (as my old football coach would say), I like to play devil's advocate. I do this right before the inspection period expires, and I only do it for larger acquisitions. But I'd recommend that newbies definitely do this—even for a house!

We (in Stewardship) have an E-(executive) Team that meets over Zoom to evaluate every deal a partner submits. Having extra eyes on deals helps you fight confirmation basis and ignore contrary evidence that the deal might not be that good. Here's three examples of those submittals by Noah Gilliom from Indianapolis using Loom.com:

516 W. Noble St.: https://tinyurl.com/y4n7prnc
2235 Spann Ave.: https://tinyurl.com/y6rzyrjn
291 Pokagon Dr.: https://tinyurl.com/y5f5mjqt

Always be willing to walk away, and never become emotionally attached to a property. At the end of the day, it's just an investment. No one becomes emotionally attached to their GE stock. (I hope!) And despite being under contract, until the ink is dry on the settlement statement and the deal is funded, you're still in negotiations.

Summary of the Process

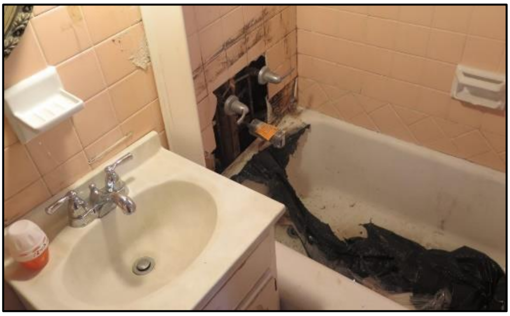
Some parts of real estate investing are a lot of fun. Some aren't. Due diligence requires time, effort, and attention to detail—but it's absolutely worth it. Not only will it save you from costly mistakes, but it will also provide you with opportunities to get even better deals.

Furthermore, many new investors struggle with confidence and are scared to death going into their first deal. Knowing how to perform thorough due diligence can alleviate much of that fear.

Nothing is entirely certain in real estate investing (or life!), but due diligence can provide a much higher level of assurance.

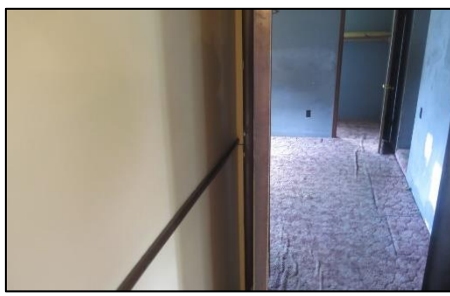
Let's Detail an Example

In this example, the property in question was in an area that we knew well and had several rentals. Therefore, we were comfortable with the location and felt we knew rental prices.



But as I've noted when discussing our BRRRR strategy, we strive to be all in on a property for 75% of its market value in order to refinance out our entire investment. So, the big issue for to us is the ARV.

This house was a 4-bed/2.5-bath. It was bank owned and in rough shape. So, just about everything needed redone. There was an additional half bathroom in its finished basement; however, finishing your basement almost never makes sense. If it's already finished and dry when you buy it, it's a bit of a bonus.



As you can see, it needed work. The property, though, was listed for just $49,000. (We bought it several years ago.) As for comps, here's what our real estate agent sent me regarding nearby houses with three to four bedrooms and two to three bathrooms that were built between 50 and 75 years ago. All the properties had sold in the last six months.

Residential Single Line

Subdivision	Area	Price	Type	Bd	Bth	Plan
[redacted]	205	$32,000	Single	2	2	Ranch
	205	$36,400	Single	3	2.1	Ranch
	205	$39,000	Single	3	2	Ranch
	205	$51,750	Single	3	2	Raised Ranch
	205	$58,000	Single	2	2	Ranch
	205	$60,000	Single	3	2	Ranch
	205	$82,000	Single	3	2	Side/Side Split
	205	$81,000	Single	3	2.1	Side/Side Split
	205	$78,000	Single	4	2	Ranch
	205	$72,500	Single	4	2.1	Side/Side Split
	205	$93,000	Single	3	2	Ranch
	205	$97,000	Single	3	2	Ranch
	205	$104,500	Single	3	3	Ranch
	205	$114,900	Single	5	2.1	Ranch
	205	$125,000	Single	4	3	Ranch
	205	$124,000	Single	3	2.1	Raised Ranch
	205	$133,500	Single	4	2.1	Side/Side Split

Prices ranged widely to say the least! So, while this type of list from the MLS is helpful, it's far better to export the list into Excel and then manually go through and make adjustments from the comps.

When we purchased this property, the market still had a lot of foreclosures. There were several real estate owned properties (REOs) on this list, and each was in terrible condition.

Those properties would not be comparable to our finished product. Neither would houses that were much worse, better, smaller, or bigger. I went through the list and removed anything that shouldn't be there. Then, I calculated the average of those that were left, along with average price per square foot, and compared that to the subject property's square footage. It looked like this:

PRICE	PRICE_SALE	DATE_COE	BDRMS	BATHS_TC	SQFT	AGE_DESC	GAR_PRK_	BASEMEN	TYPE_OF_OWNERSHIP	Notes
41,500			4	2.1	1536	51-75 Years	1	Finished	REO	
36400	36400	1/8/2016 0:00	3	2.1	1586	51-75 Years	0	Finished,	REO	
44520	39000	7/20/2015 0:00	3	2		51-75 Years		Not Finish	REO	
51750	51750	10/13/2015 0:00	3	2		51-75 Years	1	Concrete	Private	Short Sale, bad shape
63600	60000	9/30/2015 0:00	3	2		51-75 Years		Finished,	HUD	
80000	82000	12/28/2015 0:00	3	2	1056	51-75 Years	2	Concrete,	Private	
84500	78000	9/25/2015 0:00	4	2	1529	51-75 Years	2	Concrete,	Private	
84900	72500	10/19/2015 0:00	4	2.1		31-40 Years	2	Concrete,	REO	
97000	93000	8/27/2015 0:00	3	2	1196	51-75 Years	2	Concrete,	Investor	
99000	97000	1/15/2016 0:00	3	2	960	51-75 Years	1	Finished,	Private	Too small, second bath in basement
104500	104500	11/19/2015 0:00	3	3	1200	51-75 Years	2	Concrete,	Private	
114900	114900	8/6/2015 0:00	5	2.1	960	51-75 Years	2	Daylight, I	Private	
125000	125000	8/14/2015 0:00	4	3	1563	51-75 Years		Full	Investor	
125000	124000	5/29/2015 0:00	3	2.1	1379	31-40 Years	2	Finished,	Private	
135000	133500	6/8/2015 0:00	4	2.1	1660	31-40 Years	2	Concrete	Private	Different style, too nice
Average Price		$103,057								
Price Per Sq. Ft.		$81.21								
Subject X Sq. Ft.		$124,741								

This is only the start of an analysis. It should also involve taking a closer look at each of the comparables (especially the pictures on their listings) to see what kind of shape they were in when they sold and make adjustments for basements, finished basements, central A/C, garages, carports, fenced yards, style and age of construction, and perhaps the subdivision (nearby properties may still be in better or worse subdivisions). You want to make sure each property is, if possible, in the same school district, too.

The point is to think like an appraiser and to turn each comparable property into an exact replica of what your subject property *will be* when you're finished with the rehab. That means you take money off the price of comparable sales if they have an added benefit and add money to it if they are deficient in some way.

For example, if a comparable sale is identical to yours except it has an extra bathroom, take off maybe $5,000 (depending on price and area) from its sale price, because that's what the comparable house would have sold for if it was identical to your subject property.

In this case, a closer analysis didn't change our conclusion from the original. I decided the property was worth approximately $120,000 fixed up. We offered $42,000 and came to terms at $45,000.

Once we had it under contract, I painstakingly went through the property and put together a scope of work. The scope had over 300 line items on it, just to give you an idea of how much there was to do. I added a contingency for unforeseen issues and accounted for holding costs. My rehab estimate came in at just over $40,000. But in my thorough analysis, I noticed something else…

Signs of Termite Damage

During my initial walkthrough (when I only put together a one-page sheet with a quick estimate), I hadn't noticed that some of the joists in the basement had been chewed up. However, on my thorough walkthrough after we had it under contract (which lasted over two hours), I found ample evidence that wood-devouring termites had been there and done what they do. (See the photos on page 80.)

I knew banks wouldn't simply take my word for it though. Plus, I wanted to make sure I understood the full scope of the problem. So, I ordered a termite inspection. The damage was mostly isolated to a few spots in the basement and one side of the house, so the repairs would be tolerable. Also, termite treatments themselves are pretty inexpensive. But still, the property was not in the condition we initially expected it to be.

With this new knowledge, we decided to "retrade." In other words, we would renegotiate the purchase price (or terms) based on what we found during due diligence. This is single-handedly one of the biggest advantages of doing due diligence well. We asked for $3,500 off; the bank agreed immediately. (I probably should have asked for at least $5,000 off!)

My new rehab budget came in at just over $44,000. We did end up going slightly over that budget, but fortunately, it wasn't too bad. We finished all in on the property for just over $88,000.

Fixed Asset	
1499 Investment and Improvement	
1500 Investment Inventory Asset	41,500
1502 Building Improvements	
6101 Contractors	4,150
6104 Building Materials	9,870
6105 Surveying & Inspections	100
6106 Flooring - Carpet/Vinyl	2,777
6108 Appliance/Furniture Replacements	1,955
6110 Construction Plumbing	150
6111 Extermination	600
6113 Painting	7,214
6116 Landscaping	1,420
6118 Clean out & Const Cleanup	250
6120 HVAC Instalation/Repair - Rehab	2,005
6125 Holding Costs	1,279
6126 Maintenance CB's (Capital)	13,039
6401 Gas & Propane	216
6402 Water & Sewer	571
6403 Electricity	443
6404 Garbage/Dumpster/Trash	524
1502 Total Building Improvements	46,563
1499 Total Investment and Improvement	88,063

Given that I believed the property was worth $120,000 (a few years back now), that put us all in for 73.39%. So, even with loan fees, we could refinance out just about everything we put into the property. That meant we pretty much bought that puppy for free! And in the end, it turned out to be a nice little home:

Bringing tired, old properties back to life is one of the most enjoyable parts of real estate investing for all of us, not to mention neighbors in the area! Although, I have to say, it’s that much better when you have almost 27% equity in the property!

So, do not skimp on your due diligence, folks. Don’t get lazy. Not only can due diligence prevent you from buying a bad deal, it can also save you money on the good ones.

The Art and Science of Comp'ing a Property

One of the most important things to master when analyzing a property and performing due diligence is to accurately determine its after repair value. The best way to do this (with house or duplexes at least) is a comparative market analysis.

What Is a Comparative Market Analysis?

A comparative market analysis (CMA) is just what it sounds like. It looks at similar nearby properties that have sold recently and compares their sale prices to that of the subject property. Below are "want" vs. "need" criteria for determining what should qualify as comparable properties (aka comps):

	Want	Need
Sold Date	Last 6 Months	Last 12 Months
Distance	Same Sudivision	1 Mile
Condition	Identical	Close
Bedrooms	Same	_+/-One Bed
Bathrooms	Same	_+/- Half Bath
Square Footage	_+/- 10%	_+/- 20%
Age	_+/- 10 Years	_+/- 20 Years

Of course, nothing is ever 100% in real estate. Analysis is as much an art as a science. So, for example, if you are looking at a rural property, there may not be any good comps within a mile or so that sold in the last year. You may have to look farther away.

Perhaps you're looking at one very big house in a neighborhood that has almost only small houses. You may have to compare properties that are smaller and make bigger adjustments. Or perhaps you are looking at a house where every comparable is a foreclosed property in terrible condition, and your property is the exception.

This stuff happens. In some ways, it can be an advantage. Think of it this way: the more "cookie cutter" a property is, the harder it is to negotiate on price because the value of the property is obvious.

That being said, every analysis should result in both one expected price, as well as a potential price range. For instance, let's say you estimate the value to be $145,000, with a high end of $150,000 and a low end of $140,000. Or, if the comps are really bad, you can't be as sure, so the range should be even wider. In this instance, it would be safer to say between $125,000 and $160,000.

Keep in mind that a wider range means more risk. Thus, you'll want a bigger margin. Here's a related article: *How to Determine Value on a Property By Adjusting Values on Comps*

How to Find Comps
Once you have a subject property, you should set out to find comps. The easiest method is to use the MLS, but generally you have to be a real estate agent to gain access to it (or have an agent put together).

Gaining access to the MLS is pretty much the real estate investor's equivalent of going to heaven…and you want to go to heaven, right?!

There are several other websites you can use—although it's harder to specify exactly what characteristics you are looking for. When using these sites, you'll need to do more legwork.

Zillow.com / Redfin.com / Eppraisal.com / Trulia.com / Realtor.com

Make sure not to rely on the Zestimate or Redfin estimate; they are simply not accurate. Instead, find actual comps, and put together your own estimate. Here are some characteristics of this particular home.

2 bedrooms / 1 bathroom / 772 sq. ft. / Crawl space / No garage

So, to qualify as a good comp, we're looking for properties with the following characteristics:

- **Status:** Active, Pending, Show for Backups (like Pending), Sold

I'm not very interested in properties that were withdrawn or cancelled, as their list prices could be completely unrealistic. And the most important category to look at, by far, is "sold."

- **Sold Date:** 9 months to present

We'll split the difference between six months (what I want) and 12 months (what I need).

- **Bedrooms:** 2

In this case, there are enough two-bedroom houses nearby to compare. In addition, the difference between two-bedroom and three-bedroom houses is bigger than between three and four or four and five. This is because a three-bedroom is usually the smallest any family will consider. Thus, anything less than a three-bedroom house will usually have more transient renter base or will garner less interest from potential homebuyers.

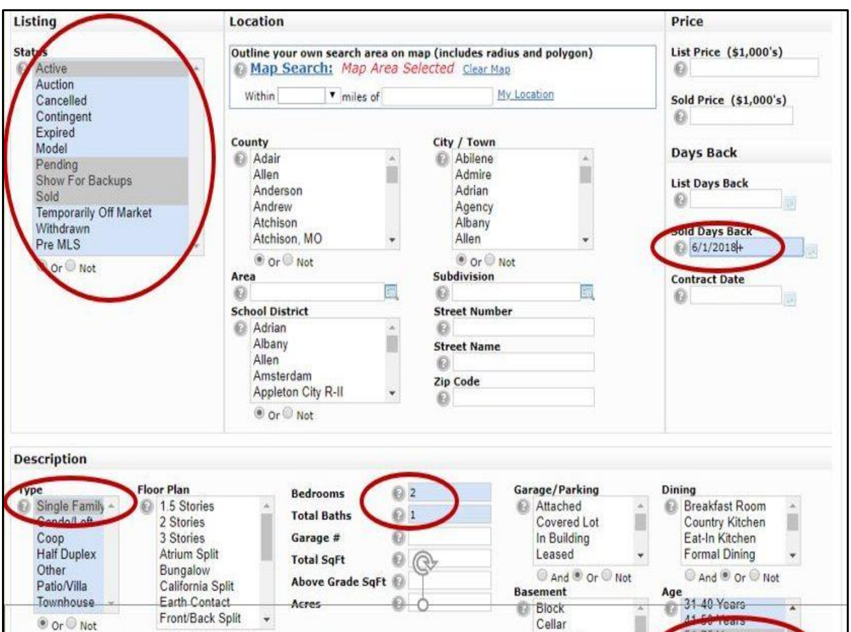
- **Bathrooms:** 1

Same as above.

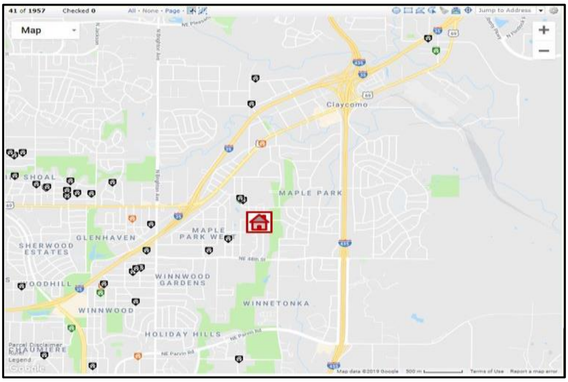
- **Age:** 50-75 years and 76-100 years

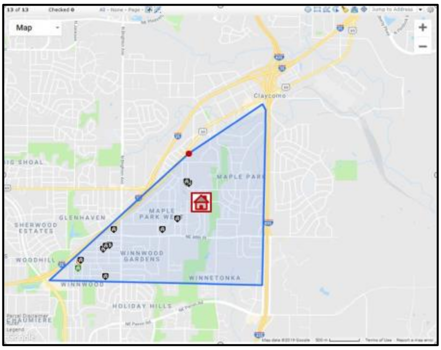
This house is 79 years old, so the above range gives me everything within about 20 years in either direction.

Here are the aforementioned screenshots from my agent of what the search criteria look like on the MLS:



Again, you need to be access to the MLS, but alternatively, you can ask your agent to search for properties for you based on certain characteristics. Next, check a map for nearby properties that fit your criteria:





Some investors and agents only consider those properties within a half-mile to one-mile radius of the subject property (the red house on the map above). We are not fans of this approach, as neighborhoods can change drastically in a short space. And this is especially true when you cross major dividing lines, such as Highway 35 on the map above. “The other side of the tracks” is an idiom for a reason. So, if you can stick to the same subdivision or group of blocks, that is preferable.

In this case, the closest properties are the best comps. But we’re more interested in the comps to the south of the subject property than those the same distance away to the west, because the ones to the west are on “the other side” of Highway 35.

You should also do an area analysis to make sure the zones in question are similar enough to each other for the comps to be useful. For example, I consider a section like the one below when conducting comparisons: While I’ll consider all the comps in that shaded area, the few next door are the ones I care about most.

Defining perimeters in this way shoots out a list of properties that you can compare in different views on the MLS. We like to export them into Excel and sometimes will have to look up certain information (like square footage) on the county website if it's not in the listing in order to fill out every cell.

We also look at the pictures and listing description to get an idea of the property's condition. (Hint: If there aren't any pictures, it almost certainly means the property is in bad shape.)

In this case, here's the spreadsheet I created:

STATUS	Number	Street	List Price	Sales Price	Sale Date	Beds	Baths	Sq. Ft.	Age	Garage	Basement	Type	Notes
Subject	[redacted]	**Beacon**	**$27,500**	**$27,500**		**2**	**1**	**773**	**76-100 Years**	**0**	**Crawlspace**	**Investor**	
	[redacted]												
Active	[redacted]	Wheeling	$45,000			2	1	558	76-100 Years	0	Partial, Walk Out	Private	
Active	[redacted]	44th	$80,000			2	1	856	76-100 Years	1	Crawl Space	Investor	
Pending	[redacted]	45th	$95,000			2	1	836	76-100 Years	0	Full, Inside Entrance	Private	
Sold	[redacted]	Wheeling	$49,500	$40,000	1/4/2019	2	1	630	76-100 Years	0	Block, Not Finished, Walk Out	REO	
Sold	[redacted]	White	$65,000	$60,000	7/27/2018	2	1	1152	76-100 Years	0	Block, Not Finished	Private	
Sold	[redacted]	45TH	$84,900	$84,900	8/23/2018	2	1	864	76-100 Years	0	Concrete, Partial	Private	
Sold	[redacted]	Lister	$90,000	$95,000	1/4/2019	2	1	824	76-100 Years	0	Block	Private	
Sold	[redacted]	Wheeling	$90,000	$80,000	1/2/2019	2	1	800	51-75 Years	2	Block	Private	
Sold	[redacted]	48th	$93,000	$100,000	7/27/2018	2	1	912	51-75 Years	0	Block, Walk Out	Private	
Sold	[redacted]	46th	$105,000	$107,500	7/25/2018	2	1	864	51-75 Years	0	Crawl Space	Private	
Sold	[redacted]	44th	$117,000	$117,000	8/24/2018	2	1	784	51-75 Years	1	Block, Walk Out	Private	
Sold	[redacted]	46th	$119,950	$119,950	2/19/2019	2	1	1290	76-100 Years	2	Concrete, Full, Inside Entrance	Investor	
Sold	[redacted]	49th	$135,000	$133,000	7/26/2018	2	1	1632	51-75 Years	1	Daylight, Finished	Private	

Then, I go through each comp and determine if it's a good comparable or a bad one. It's important to remember that I'm comparing these properties to what the subject property *will* be worth when it's fully repaired—not what it's worth in its current state.

Related: The *Investor's Guide to Pulling Realistic Rental Comps*

Good Comps vs. Bad Comps

Here's my analysis of each property listed above and the justification for deeming it a good or bad comp:

- Wheeling: **Bad**
  Only 558 sq. ft., so over 200 sq. ft. smaller
- 44th: **Good**
  80 sq. ft. bigger, similar condition
- 45th: **Good**
  60 sq. ft. bigger, garage but similar condition
- Wheeling: **Bad**
  REO—never compare a property to a foreclosed property, as they sell for less and are almost always in bad shape

- White: **Bad**
  Pictures look bad, listing says “fixer upper”
- 45th: **Good**
  90 sq. ft. bigger, similar condition
- Lister: **Good**
  50 sq. ft. bigger, similar condition
- Wheeling: **Good**
  25 sq. ft. bigger, 2-car garage but similar condition
- 48th: **Good (but barely)**
  150 sq. ft. bigger, similar condition
- 46th: **Bad (but close)**
  90 sq. ft. bigger, substantially nicer
- 44th: **Bad**
  Much, much nicer
- 46th: **Bad**
  500 sq. ft. bigger, nicer
- 49th: **Bad**
  900 sq. ft. bigger, much nicer

STATUS	Number	Street	List Price	Sales Price	Sale Date	Beds	Baths	Sq. Ft.	Age	Garage	Basement	Type	Notes
Subject	[redacted]	**Beacon**	**$27,500**	**$27,500**		**2**	**1**	**773**	**76-100 Years**	**0**	**Crawlspace**	**Investor**	
	[redacted]												
Active	[redacted]	Wheeling	$45,000			2	1	558	76-100 Years	0	Partial, Walk Out	Private	Too Small
Active	[redacted]	44th	$80,000			2	1	856	76-100 Years	1	Crawl Space	Investor	Good
Pending	[redacted]	45th	$95,000			2	1	836	76-100 Years	0	Full, Inside Entrance	Private	Good
Sold	[redacted]	Wheeling	$49,500	$40,000	1/4/2019	2	1	630	76-100 Years	0	Block, Not Finished, Walk Out	REO	Foreclosure + Too Small
Sold	[redacted]	White	$65,000	$60,000	7/27/2018	2	1	1152	76-100 Years	0	Block, Not Finished	Private	"Fixer Upper"
Sold	[redacted]	45TH	$84,900	$84,900	8/23/2018	2	1	864	76-100 Years	0	Concrete, Partial	Private	Good
Sold	[redacted]	Lister	$90,000	$95,000	1/4/2019	2	1	824	76-100 Years	0	Block	Private	Good
Sold	[redacted]	Wheeling	$90,000	$80,000	1/2/2019	2	1	800	51-75 Years	2	Block	Private	Good
Sold	[redacted]	48th	$93,000	$100,000	7/27/2018	2	1	912	51-75 Years	0	Block, Walk Out	Private	Good
Sold	[redacted]	46th	$105,000	$107,500	7/25/2018	2	1	864	51-75 Years	0	Crawl Space	Private	Too Nice
Sold	[redacted]	44th	$117,000	$117,000	8/24/2018	2	1	784	51-75 Years	1	Block, Walk Out	Private	Pictures: Too nice
Sold	[redacted]	46th	$119,950	$119,950	2/19/2019	2	1	1290	76-100 Years	2	Concrete, Full, Inside Entrance	Investor	Too Big
Sold	[redacted]	49th	$135,000	$133,000	7/26/2018	2	1	1632	51-75 Years	1	Daylight, Finished	Private	Too Big

At this point, I have six good comps. The four I’m most interested in, however, are the four sold.

How to Adjust Values on Comps

Next, we want to turn these houses into an exact replica of our subject property. So, if the property is nicer or better than ours, we *reduce* its sold price. Why? Because, presumably, if it didn’t have the feature our subject property lacks, it would have sold for less.

The opposite calculation would apply if our property has features the comp does not. For example, one of the properties on 45th has window A/C units, but our property will have central air. I will *add* $2,500 to 45th's sale price as an adjustment to what it would have sold for (at least what I *think* it would have sold for) if it had A/C.

But how much should these adjustments be? There's no magic formula. The best explanation I've seen was in a Sacramento appraisal blog:

Compare houses in a neighborhood to determine the adjustment. Or in other words, find matched paired sales to discover what buyers are willing to pay for a certain feature. For instance, if you find a house that sold at $230,000 at 1,700 sq. ft., but a very similar house sold at $220,000 at 1,500 sq. ft., that tells us the market paid an extra $10,000 for 200 extra square feet. In this case the adjustment for sq. ft. would be $50 per sq. ft. since $10,000 divided by 200 equals $50 per sq. ft. This is just one example though. It's important to find several other matched pairs so you can make a reasonable judgement about what the market is willing to pay for extra square footage.

Again, it's not going to be perfect. The goal is simply to be very close. Let's walk through the 45th property together.

- **45th Sale Price: $84,900**
  Subject / 45th / Adjustment:
- Beds: 2 / 2/ **$0**
- Baths: 1 / 1 / **$0**
- Sq. Ft: 773 / 864 / **-$5,000**
- Condition: Good / Fair / **+$5,000**
- Basement: No / Yes / **-$2,500**
- Garage: No / No / **$0**
- Sale Date: 3-15-2019 / 8-23-2018 / **+$2,500** (the market appreciated in the interim)
- HVAC: Central / Window / **+$2,500**
- Sum: **+$2,500**
- Adjusted Price: **$87,400**

You should also look out for seller concessions. Oftentimes, the seller will make a concession of a few thousand dollars, usually to help the buyer with financing. If such a concession exists, it will not be taken out of the sold price but will simply be noted at the bottom of the listing. Subtract that amount from the sale price.

Mod Dt:	07/25/2018	Entry Dt:	05/14/2018
Cont Dt:	06/07/2018	Close Dt:	07/25/2018
Agency:	Designated Agent	DUC:	48
Financial Concessions:		$5,000.00	
Incentives:			

Here's the breakdown for each of the four sold comps:

Comp		Suebject	Adjustment	
45th	$84,900			
Beds	2	2	$0	
Baths	1	1	$0	
Sq. Ft	864	773	($5,000)	
Condition	Fair	Good	$5,000	
Basement	Yes	No	($2,500)	
Garage	No	No	$0	
Sale Date	8/23/2018	N/A	$2,500	
HVAC	Window	HVAC	$2,500	
Sum			**$2,500**	**$87,400**
Comp				
Lister	$95,000			
Beds	2	2	$0	
Baths	1	1	$0	
Sq. Ft	824	773	($2,500)	
Condition	Good	Good	$0	
Basement	Yes	No	($2,500)	
Garage	No	No	$0	
Sale Date	1/4/2019	N/A	$0	
HVAC	HVAC	HVAC	$0	
Sum			**$0**	**$95,000**
Comp			**Adjustment**	
Wheeling	$80,000			
Beds	2	2	$0	
Baths	1	1	$0	
Sq. Ft	800	773	($1,000)	
Condition	Fair	Good	$5,000	
Basement	Yes	No	($2,500)	
Garage	2	No	($3,500)	
Sale Date	1/2/2019	N/A	$0	
HVAC	Winow	HVAC	$2,500	
Sum			**$500**	**$80,500**
Comp				
48th	$100,000			
Beds	2	2	$0	
Baths	1	1	$0	
Sq. Ft	864	773	($5,000)	
Condition	Good	Good	$0	
Basement	Walkout	No	($3,500)	
Garage	No	No	$0	
Sale Date	7/27/2018	N/A	$2,500	
HVAC	HVAC	HVAC	$0	
Sum			**($6,000)**	**$94,000**

The four adjusted values are:

- 45th: $87,400
- Lister: $95,000
- Wheeling: $80,500
- 48th: $94,000
- **Average: $89,225**

In addition, we looked at price per square foot and compared that to our subject property:

- 45th: $98.26
- Lister: $109.22
- Wheeling: $112.50
- 48th: $101.97
- **Average: $105.49**

At $105.49, the subject property would be worth = $81,544. (Here's the math: 773 x $105.49 = $81,544.)

From this analysis, we'd estimate the property to be worth between $80,000 and $95,000, with the sale price likely falling between $85,000 and $90,000.

If flipping, we might list it at $94,900 just to see if that would elicit an offer, but we would expect it to sell for a bit under $90,000.

CMA Pro Report

These pages give a general overview

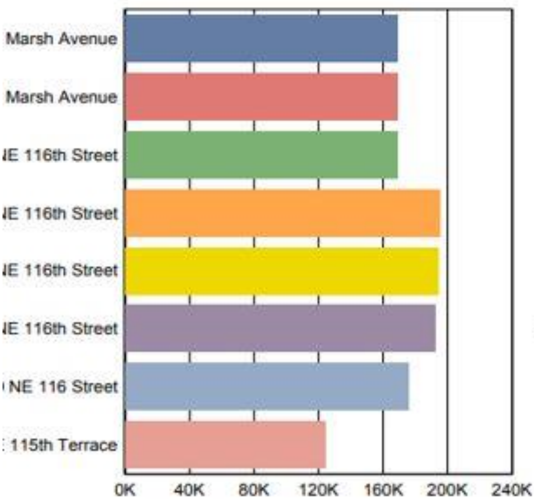
Sold Properties

Total # of Listings	8
Lowest Price	$124,000
Highest Price	$195,000
Average Price	$173,404
Avg. Price/SqFt	$96.63
Avg DOM	244

Professional CMAs and Appraisals

Of course, you can also ask your real estate agent to put together a CMA, which will have all sorts of information, including side-by-side comparisons and fancy charts.

Here are a couple examples:



Just make sure your agent and you perform the analysis as described above. Fancy charts are nice and all, but "garbage in equals garbage out" in terms of data. And don't waste an agent's time by requesting one CMA after another on properties you aren't serious about.

Indeed, brokers often charge for detailed CMAs (where they do site visits) called broker price opinions (BPOs), so they'll quickly grow tired of running free comps for you if you don't buy anything.

Finally, you can get an actual appraisal—and will need to if financing is involved. Usually, an appraiser will select three comps to analyze. We select as many as you believe are good (though rarely over five or six for comparison sake).

Here is what a sample appraisal (from the first two pages) looks like:

Address	Kansas City, MO 64137	Kansas City, MO 64134		Kansas City, MO 64134		Kansas City, MO 64134	
Proximity to Subject		0.42 miles E		0.96 miles S		0.72 miles NE	
Sale Price	$		$ 94,000		$ 89,000		$ 87,100
Sale Price/Gross Liv. Area	$ sq. ft.	$ 85.14 sq. ft.		$ 92.71 sq. ft.		$ 63.39 sq. ft.	
Data Source(s)		County,HrtLd,MLS#2098337		County,HrtLd,MLS#2052492		County,HrtLd,MLS#2096543	
Verification Source(s)		KCDS		KCDS		KCDS	
VALUE ADJUSTMENTS	DESCRIPTION	DESCRIPTION	+(-)$ Adjustment	DESCRIPTION	+(-)$ Adjustment	DESCRIPTION	+(-)$ Adjustment
Sale or Financing		Cash		VA		Conventional	
Concessions		$2,820 Seller	-2,820	$2,000 Seller	-2,000	None Reported	
Date of Sale/Time		5/2018		9/2017		4/2018	
Location	Moreland Heights	Skyline Heights		Stratford Estates		Fairlane	
Leasehold/Fee Simple	Fee Simple	Fee Simple		Fee Simple		Fee Simple	
Site	10,465 +/- sq. ft.	8,400 sq. ft.		9,660 sq. ft.		9,072 sq. ft.	
View	Residential	Residential		Residential		Residential	
Design (Style)	Raised Ranch	Split Level		Raised Ranch		Split Level	
Quality of Construction	Typical for area	Typical for area		Typical for area		Typical for area	
Actual Age	60	58		48	-2,000	64	
Condition	Good	Good		Good/Average	+2,000	Average	+4,000
Above Grade	Total / Bdrms. / Baths	Total / Bdrms. / Baths		Total / Bdrms. / Baths		Total / Bdrms. / Baths	
Room Count	6 / 4 / 1	5 / 3 / 1		5 / 3 / 1		7 / 3 / 2	-2,000
Gross Living Area	1,212 sq. ft.	1,104 sq. ft.	+3,200	960 sq. ft.	+7,600	1,374 sq. ft.	-4,900
Basement & Finished	Partial No Walk out	Full No Walk out	-1,000	Full Walk Out	-3,000	Full No Walk out	-1,000
Rooms Below Grade	No Finish	205 sq. ft. finish	-2,000	461 sq. ft. finish	-4,600	218 sq. ft. finish	-2,200
Functional Utility	Average	Average		Average		Average	
Heating/Cooling	F-Air/Cent-Air	F-Air/Cent-Air		F-Air/Cent-Air		F-Air/Cent-Air	
Energy Efficient Items	Typical	Typical		Typical		Typical	
Garage/Carport	1 Built in	1 Built in		2 Built-In	-2,000	1 Built in	
Porch/Patio/Deck	Deck	Patio/Fence	-1,000	Covered Deck	-500	Patio/Fence	-1,000
Fence/Spk/Pool							
Fireplace	None	None		None		2 Fireplaces	-2,000
Net Adjustment (Total)		+ X -	$ -3,620	+ X -	$ -4,500	+ X -	$ -9,100
Adjusted Sale Price		Net Adj. 3.85 %		Net Adj. 5.06 %		Net Adj. 10.45 %	
of Comparables		Gross Adj. 10.66 %	$ 90,380	Gross Adj. 26.63 %	$ 84,500	Gross Adj. 19.63 %	$ 78,000

In case you are wondering, the value this appraiser arrived at for the subject property was $85,000.

Entrepreneurs aren't necessarily number crunchers. But "running the numbers" is a critical skill to master if you want to be successful. When it comes to comparing properties and determining values, it's critical to think like an appraiser. This is not only essential when identifying good comps or performing due diligence, but also when making appropriate adjustments and landing on a realistic estimate of value.

You can't make good decisions without good numbers! So, it's important to put in the work required to get there.

CHAPTER 6
ACQUISITON, PART 3: NEGOGIATING THE DEAL

BRRRR: Buy—**R**ehab—**R**ent—**R**efinance—**R**epeat

- **1st BASE**
  —Acquisition

Every real estate guru has been saying this since the days of William Nickerson and before: *Always build rapport!* It might seem obvious, but it's hard to understate just how important rapport is when it comes to real estate or any other business. Still, many of us shrug it off.

Of course, this is not necessary if we're bidding at the courthouse for foreclosures or online. That's simply a numbers game. But mostly we'll be dealing with real flesh and blood human beings and the principles of *How to Win Friends and Influence People* should be our guide.

In his book *Influence*, Robert Cialdini simply calls rapport-based negotiations the "the liking rule." He describes an illuminating example:

There is a man in Detroit, Joe Girard, who specialized in using the liking rule to sell Chevrolets. He became wealthy in the process, making hundreds of thousands of dollars a year. With such a salary, we might guess that he was a high-level GM executive or perhaps the owner of a Chevrolet dealership. But no. He made his money as a salesman on the showroom floor. He was phenomenal at what he did. For twelve years straight, he won the title of "Number One Car Salesman"; he averaged more than five cars and trucks sold every day he worked; and he has been called the world's "greatest car salesman" by the Guinness Book of World Records.

For all his success, the formula he employed was surprisingly simple. It consisted of offering people just two things: a fair price and someone they liked to buy from. 'And that's it,' he claimed in an interview.

'Finding the salesman you like, plus the price. Put them both together, and you get a deal.' (Cialdini 146).

Again, this ain't rocket science. Think to yourself whether you would be willing to buy something—even something you wanted to buy—from someone who was being a complete jerk. Almost just to spite him, wouldn't you try to buy it from someone else?

But even more so than just not being a jerk, it's important to be proactive in your friendliness. Indeed, never underestimate the power of genuine compliment—although we're not referring to false flattery. For one, false flattery is, well, false and thereby dishonest. But in addition, most people can see right through it and it comes off as fake and manipulative. False flattery does much more harm than good.

Cooperation

There's a reason that so many business deals are done on the golf course. People want to do deals with people they like, and doing fun activities together increases such positive feelings toward one another (presuming the game isn't too intense, of course).

We need to remind ourselves not to be in too much of a hurry. Say you're looking at a house with a potential seller. Go ahead and shoot the breeze for a few minutes beforehand. Talk about anything other than the property. Be genuinely interested in what they have to say.

Also, don't be afraid to compliment them. If the seller notes a personal achievement, go ahead and compliment (even if they are obviously fishing for compliments). If there's a nice piece of artwork or something like that in the home, go ahead and say so.

And while we wouldn't generally compliment the house (because you are trying to get a good deal and that would also put you at a disadvantage), we also wouldn't insult it or say anything the owner may take offense to. It's their house and many will feel personally insulted if you say something negative, even if it's no reflection on them.

Overall, it's a very simple lesson; people like to sell and buy from people they like. But while it's simple, it's often ignored. Never forget to always build rapport.

Seven "No's" are Halfway to a "Yes!"

Back when I (Andrew) was in college, I had a class on negotiations, and one of the main projects was called "collecting no's." Basically, we had to get rejected 10 times. Each request had to be realistic, legal and to someone who didn't know you were asking it as part of an assignment. The goal was to collect at least 10 "no's" and write them each down and turn in that notebook.

The whole point was simply to break down the fear of rejection. Salespeople will sometimes talk as if they have to go through X number of "no's" to get a "yes" based on what percentage of their leads they actually convert. So, every "no"—while technically accomplishing nothing—psychologically feels like moving forward to a "yes." So, the idea of this assignment was, after failing to convince my roommates to move my furniture for me and the like, the fear of hearing "no" was eradicated from me.

Well, not completely. Getting rejected sucks, but generally it's the fear of that rejection that's the worst thing. I'm not talking about being rejected by a spouse or parent or someone really close to you, but in the smaller things. And with those things, it really shouldn't matter if you're rejected. This is particularly true for real estate investment. It may feel personal, but it's just business; just about the offer.

While it may be easy to tell yourself that it doesn't matter if some seller rejects you, it's a lot harder to actually feel that way. I certainly have by no means mastered this, but I can say it helps to consciously remind yourself beforehand of how little it will matter in a month (or in a week, or tomorrow for that matter, or in 10 minutes) if some seller gets offended because they think your offer is too low.

Imagine detaching yourself from the situation and seeing it as a third party, neutral observer. Take the emotion out of it, as well as the potential for hurt feelings or embarrassment. If they get offended or angry or reject you, who cares?

What would that third-party observer think? Well, such a person would probably be bored out of their mind. Watching two people negotiate a deal you have no stake in (and aren't trying to learn from) is about as interesting as watching paint dry.

And, of course, each time it gets easier. So keep at it, and that sense of calm during negotiations will come, at least to a large extent. At first, however, you will just have to accept the butterflies. I think it's best not to try to overload yourself with various negotiating techniques and what not to do when approaching negotiating early on. Instead, focus on the key components until you master them.

And they boil down to two things:
1. Ask for what you want
2. Always be willing to walk away
Let's examine these elements in more depth.

Two Key Components for Your Negotiations

1. Ask for What You Want

Some years back, my father was locked in a negotiation to purchase a house and had reached his strike price. Problem was that he and the seller were still $10,000 apart. He was firmly at $170,000, and she was stuck at $180,000.

Earlier in the conversation, however, the seller had mentioned how her son needed a new cell phone (in the days before smart phones). Well, my dad just happened to have an extra one (that he was going to give to me, by the way). All of a sudden, a solution appeared.

"How about this? I happen to have an extra cell phone—how about I throw it in if you can come down to $170,000? Does that work?"

And she said yes. One cellphone for $10,000.

This story obviously highlights the importance of building rapport, but it also shows how critical it is to simply ask for what you want. The offer was kind of ridiculous, but what was the harm in it? After all, my dad had reached his strike price, there was no going up, so if no creative (or ridiculous) solution could be found, the deal was lost.

I've heard many investors say that if you're not embarrassed about your first offer, you're offering too much. And there's certainly a lot of truth in that much of the time.

But a better way to think of it is this: just ask for what you want.

In the case of real estate, that equals what you need to make it a good deal (with room to negotiate included, of course). If you're afraid to ask for what you want, you'll either pay too much or offer so close to your strike price that there won't be any room to negotiate, and you'll probably lose a few deals you would have otherwise gotten.

I've noticed time and time again that most things are negotiable and just asking, "Do you have any flexibility on price?" is all it takes to get at least some sort of discount. So ask for what you want.

2. Always Be Willing to Walk Away

Sometime back, I (Andrew) was traveling in South America with a good friend of mine who is fluent in Spanish. My Spanish at the time was *no bueno,* so I was fairly reliant on him when it came to communicating with the locals.

I had somehow forgotten my sunglasses, and so we walked to buy some at one of the various shops. I picked up the pair and asked how much. The shopkeeper told me, and then my friend said (in English) to ask how much he would come down. He offered a token discount. Then my friend told me to set the sunglasses down and walk away. So I did. The guy grabbed my arm and cut his price substantially.

"Ask for more," said my friend. At the end of the day, I bought the sunglasses for half of what they were going for.

Such bartering is par for the course in Latin America, but it highlights a major lesson: The power to walk away is crucial. In some ways, it's defeating the fear of rejecting. Regardless, it is of the utmost importance to never be a motivated buyer (or seller for that matter).

With few exceptions (1031's and the like), there little urgency to buy again. The next good deal will come; give it time. With selling, there are certainly more reasons to be motivated, but fight it like the plague. You should have your strike price set before the negotiation begins, and stick by that with unrelenting fervor. Any participant who is not willing to walk away is at an enormous disadvantage and will get the short end of the stick almost every time.

Talk less, Listen More…A Lot More!
There are two major components to negotiating that make it wise to talk less rather than more. The first is that by actively listening, you build trust and rapport with the seller. The other is because the more you talk, the more likely you are to give something away that weakens your hand and the less likely the other side will.

In one instance, my brother and I (Andrew) were negotiating to buy a property and the seller just loved to talk and talk. The conversation went for close to two hours before we got down to business. But in this time, we learned valuable information—for example, that he had a previous buyer fall out and was more concerned about our ability to close than getting top dollar. Knowing this, we were able to highlight our financial ability to close in our pitch and come in a bit lower than we might have otherwise.

Negotiating is not an easy thing to master but each success builds on itself. For those looking for more sophisticated techniques, *Getting to Yes* and *Influence* are great books to check out. But as far as the foundation goes, defeating the fear of rejection is the key first step.

Mastering a Negotiator's Mindset

When it comes to listening more and talking less, I've (Andrew) yet to come across a book on this topic as helpful as *Never Split the Difference* by former FBI hostage-negotiator Chris Voss.

As one might suspect, a hostage negotiator doesn't exactly get the option of splitting the difference. Instead, Voss digs deeper into human psychology, all the while highlighting how these various techniques work with practical anecdotes from both hostage negotiating and business.

Voss notes that classic negotiating books such as *Getting to Yes* had a lot of great advise in them—particularly with regards to negotiating based on interests instead of positions (which devolves into bartering back and forth over price) and trying to find win-win solutions where possible.

But advances in our understanding of psychology (which are best highlighted in the great book *Thinking Fast and Slow)* and real-world experience doesn't always follow the textbook theories. Voss then combines the practical and scientific for a tour-de-force book on negotiating.

First off, the most important part of negotiating is to go in with the right frame of mind. As Voss puts it, *People who view negotiation as a battle of arguments become overwhelmed by the voices in their heads. Negotiation is not an act of battle, it's a process of discovery. The goal is to uncover as much information as possible. To quiet the voices in your head, make your sole and all-encompassing purpose the other person and what they have to say.*

Instead of a battle, *The language of negotiation is primarily a language of conversation and rapport.* This "language" includes smiling and being positive and friendly. This is important because it puts both of you in a positive frame of mind; you both are "more likely to collaborate and problem solve instead of fight and resist." In fact, just slowing down can aid the process of rapport building. If you go to fast, you will 1) skip most opportunities to build rapport, and 2) make people feel like they are not being heard, and thus they may get defensive.

After you've slowed things down and built rapport, the next mind frame change is: "Don't commit to assumptions. Instead, view them as hypothesis and use the negotiation to test them rigorously." The idea here is that instead of trying to barge your way to some conclusion, see the negotiation as a fact-finding mission. This will take much of the pressure off, but it also puts you at the advantage.

The person who talks more, loses. The person who listens more, wins. This is because the person who's talking is giving up information that could be useful in figuring out if a deal makes sense. Maybe, for example, a seller will let loose that they need to sell very quickly, and would thereby consider a lower price—or maybe they have the ability, and thus possibly the willingness, to owner finance. Or perhaps they have another property to sell. If you're too busy talking, you may miss these valuable insights. There is much more to gain from Voss book and I would recommend getting his book *Never Split the Difference*.

Use Interest-Based Negotiation to Close True Win-Win Deals

Interest-based negotiations are sometimes called "win-win negotiations," which all of us have heard more than a few gurus and self-help authors go on about. Indeed, some of us may have even developed a sort of Pavlovian rolling-of-the-eyes response to such external stimuli.

However, interest-based negotiating is much more in-depth and useful than the feel-good "win-win" negotiations we hear about so much. The idea behind interest-based negotiations is simply to figure out what the other person wants or needs so you can come to an agreement (or not) based on the best fit of your needs and theirs.

Interest-based negotiations comes in contrast to position-based negotiations. A position is based on a need, but is explicit. So, for example, an interest is "I want to get as much money as I can from this sale," whereas a position is "I want to sell the property for $350,000." A good rule of thumb to differentiate the two is that if a specific name or number is mentioned, it is a position.

The advantage with interest-based negotiations is that almost every seller or buyer has more than one interest, and there are often many ways to satisfy any given interest, whereas there's usually only one way to satisfy a position. Here are a few examples of interests in a typical real estate transaction:

- Price
- Concessions
- Financing (i.e. seller financing, cash offer financed offer)
- Terms of seller financing if applicable
- Time to close
- Earnest money
- Likelihood of close (how strong is the buyer)
- Creative contracts (subject to, contract for deed, etc.)

The website BeyondIntractability.com gives a good illustration of how the position-based versus interest-based approaches differ:
Positional Bargaining (PB): Disputants are adversaries. Integrative [Interest-Based] Bargaining (IB): Disputants are joint problem-solvers.

IB: Goal is wise decision.
PB: Demand concessions.
IB: Work together to determine who gets what.

When to Use (and When Not to Use) Interest-Based Negotiating
First and foremost, I (Andrew) should give you a disclaimer: There are times when it doesn't make sense to use interest-based negotiating techniques. As reactionary as it may sound, there are times when a simple "win-lose" negotiation technique is the best way to go—although referring to the other side as "losing" is not necessary.

This is true when you're making an offer on a property you don't want or are just making rapid-fire lowball offers. In these cases, sitting down to determine the interests of the seller will likely just take too much time. Generally speaking, the bigger or more important the deal, the more useful interest-based negotiations are.

How to Analyze Interests

The first thing to do is to simply figure out who the stakeholders are and what their interests are. Sometimes, there may be more stakeholders than just you and the party you are buying from or selling to. For example, an anchor tenant at a retail property could be an subsidiary or "non-essential" stakeholder.

	Stakeholders	
Issues	Me	Seller
Price	Low	High
Concessions	Low	High
Strength of Buyer	N/A	Strong
Time of Sale	Whenever	Quickly
Financing	Seller Financing	No Seller Financing
Financing Terms	Low Rate, Long Term	High Rate, Short Term

To do this, make a chart that looks something like this. As you can see, we mostly disagree on our interests, but not everywhere. You want to then highlight in one color which interests are the same, which are opposite, and which are different but don't conflict. That would look like this:

	Stakeholders	
Issues	Me	Seller
Price	Low	High
Concessions	Low	High
Strength of Buyer	N/A	Strong
Time of Sale	Quickly	Quickly
Financing	Seller Financing	No Seller Financing
Financing Terms	Low Rate, Long Term	High Rate, Short Term
	Same	
	Opposite	
	Different	

After that, you want to figure out which interests are something you can't do without or the seller can't and which are wanted but not crucial. The best way to move forward is to give on issues that aren't crucial to you and get in areas that are. In the next graph, issues listed in bold and underlined are items you and seller find essential.

	Stakeholders	
Issues	Me	Seller
Price	Low	High
Concessions	Low	High
Strength of Buyer	N/A	Strong
Time of Sale	Quickly	Quickly
Financing	Seller Financing	No Seller Financing
Financing Terms	Low Rate, Long Term	High Rate, Short Term
(green)	Same	
(red)	Opposite	
(blue)	Different	

As you can see, in this scenario the seller doesn't want to give seller financeing, but may be willing to do so and do so with good terms at the right price. The things he really cares about are closing quickly (which you agree on), selling to a strong buyer (which you are), and price. While you want the lowest price on this property, great terms on seller financing may make it work. So this analysis shows you where the best places to come up with actions are.

Of course, all this depends on knowing what the other party wants, which makes fact-finding all the more important. To do this, you want to ask yourself, "What does each stakeholder care about?" And then you need to talk to them to figure it out. Luckily, since you can do this while building, it allows you to hit two birds with one stone.

Actions and Alternatives

After determining interests, you want to brainstorm potential actions (something that satisfies an interest, i.e. offer $225,000 or ask for a "subject to" purchase). You should withhold judgement and only analyze the effects of each action would have on each stakeholder's interests afterward brainstorming.

You should also analyze alternatives or things a stakeholder could do if no agreement is reached. For example, a seller could let his house be foreclosed on instead of selling. Knowing these alternatives can be very helpful, as highlighting them during a negotiation can clarify that your offer may not be perfect, it's better than any alternative.

In a deal where we purchased a 32-unit apartment complex (which I describe here), we were mostly interested in price. On the other hand, the seller needed to get out of it and had just had a seller fall through, so he was very interested in the strength of the buyer.

In our long conversations with him, this became clear, so all it took was a lot of time and energy to prove we were a strong buyer who could purchase the property and wouldn't walk away. That was enough to convince him to sell it to us at a substantially lower price than he was originally asking. The fact that his alternative was to wait for another buyer, and he had had quite enough of that was probably what allowed us to purchase that property.

Conclusion

Abraham Lincoln once said, "Give me six hours to chop down a tree, and I will spend the first four sharpening my axe." Preparation is critical, and that's as true in negotiations as anything else.

In addition to good preparation, the interest-based negotiation model allows you to work on the same side as the other party to find a solution rather than as antagonists. This will usually result in better agreements and is far less likely to lead to hostility between the parties. In other words, it's a win-win.

Use the Scarcity Principle to Your Advantage

I've (Andrew) been to more than a few events from the so-called "real estate gurus," and their final pitches always go something like this:

You can get my program for three easy payments of $2,997.00. But, oh wait, for today and today only, I will throw in this bonus three-ring binder full of all my super tips. But, wait, if you buy today, and - only, you can get it for only two payments of $997.00.

Remember, today only. In fact, you must buy it before my presentation ends. Go ahead and get up and run to the back and give us your credit card informa-tion right now. But, oh wait, if you pay today, err, I mean before this presentation ends, and before it ends only, I will throw in three free consultations with me or one of my assistants or perhaps a virtual assistant I hired in Thailand who sort of speaks English.

While my description is rather self-indulgent (and yes, there are some good gurus), the standard pitch of such gurus highlight the importance of scarcity in negotiating and sales. These gurus are basically saying, “Today is your only shot at getting this deal, so you better jump at it!” And love it or hate it, it works.

Indeed, one of the key rules of sales is that “you must always be willing to walk away.” This in and of itself highlights the principle of scarcity, because if the seller of buyer knows you are on the hook, then they will know they have all the leverage. They have at least one buyer or seller. But if you’re willing to walk away, they may have one buyer or seller, or they may have none at all and be forced to start over in their search to make a deal.

Again, we turn to Robert Cialdini and his great book *Influence: People seem to be more motivated by the thought of losing something than by the thought of gaining something of equal value. For instance, college students experienced much stronger emotions when asked to imagine losses as opposed to gains in their romantic relationships or in their grade point averages. Especially under conditions of risk and uncertainty, the threat of potential loss plays a powerful role in human decision making* (Cialdini 200).

One example Ciadini gives is health: *Health researchers Alexander Rothman and Peter Salovey have applied this insight to the medical arena, where individuals are frequently urged to undergo tests to detect existing illnesses (e.g. mammography procedures, HIV screenings, cancer self-examinations). Because such tests involve the risk that a disease will be found and the uncertainty that it will be cured, messages stressing potential losses are most effective… For example, pamphlets advising young women to check for breast cancer through self-examinations are significantly more successful if they state their case in terms of what stands to be lost rather than gained* (200).

As a matter of fact, this antipathy towards losses is such an ingrained part of human psychology that assets are actually valued to reflect this, particularly in the stock market. Part of the way stocks are valued is what is called the "beta." As Investopedia explains:

"Beta is a measure of the volatility, or systematic risk, of a security or a portfolio in comparison to the market as a whole […] A beta of 1 indicates that the security's price moves with the market. A beta of less than 1 means that the security is theoretically less volatile than the market. A beta of greater than 1 indicates that the security's price is theoretically more volatile than the market. For example, if a stock's beta is 1.2, it's theoretically 20% more volatile than the market."

The higher the volatility (or beta), the higher the necessary return. But wait a minute. Over the long run, doesn't the market go up? As the Wikipedia article on beta notes, "Academic theory claims that higher-risk investments should have higher returns over the *long-term*." In essence, because of the natural human aversion to loss and thereby aversion to risk, less volatile stocks will be worth more than more volatile stocks even if the expected return is the same.

Censorship

This longing not to lose out also plays a roll in any debate regarding censorship. As any parent knows, the best way to make your child want to do something is to tell your child that said thing is not allowed.

Turning again to Cialdini:

…The results of the few studies that have been done on censorship are highly consistent. Almost invariably, our response to banned information is to want to receive that information to a greater extent and to become more favorable toward it than we were before the ban (210).

Effectively, censorship creates an artificial scarcity that increases the perceived value of whatever is being censored. Social activists and politicians should take this psychological trait into account when discussing any attempt to censor hate speech, pornography, or other such things. Aside from important concerns over freedom of speech, such attempts may very well backfire.

Scarcity and Real Estate Investment
Every real estate investor knows that an important key to finding good deals is finding motivated sellers. The reason is simply that the seller fears missing out on a chance to get rid of the property more than missing out on getting a good price, so there's an opportunity there. And as mentioned above, in any negotiation, you always need to be willing to walk away. You never want to be a motivated seller or a motivated buyer for that matter.

Don't fall in love with a house or apartment or deal or anything. They're just investments; don't become attached.

And remember this concept outside of simply buying and selling properties. In salary negotiations with employees (or employers), you should be at least willing to walk away. Or at the very least, be willing to bluff a little about it. You can also use limited time offers for rentals (first month off or something like that). And merely the act of getting more than one bid from a contractor creates a sense of scarcity in that contractor's mind that they very well might not get this job. That should get a better price. Even with contractors you've used for a long time, it's not a bad idea to reject their quotes every once a while, just to keep them honest.

Indeed, there are a thousand uses of the scarcity principle. The important thing is simply to remember it exists, both when selling and when being sold.

Be Counterintuitive: There are times to make the first offer.

It is almost taken as a fundamental truth of negotiating that he who speaks first loses. It is axiomatic among many in business that you should try to get the other party to state their \price first, no matter how awkward it becomes. The reason for this is because it acts effectively as the first concession and perhaps tilts the deck in the other party's favor.

For example, the first offer could be way lower than the other would pay and thereby provide a huge boon. One business professional gives the example of a garage sale to illustrate this kind of thinking.

"OK, now we've met the seller. There's no price tag on the table, so here's how negotiations could go.

Scenario one:
You: I'll offer you $20 for this table.
Them: I'd like to get $35 for it.
You: Would you take $25?
Them: $30 and you've got a deal.
You: OK, deal.

Scenario two:
You: How much are you asking for this table?
Them: I'd like to get $35 for it.
You: I can't pay more than $20.
Them: Well, I could come down to $25.
You: Great, I'll take it."

Now, there's certainly a time and place for this. Sometimes you don't want to make the first offer, but it's not true that you never want to make the first offer. In fact, I would argue that when the seller is motivated, you usually do.

The reason for this boils down to two things: 1) Many sellers, even those who are motivated, have a completely unrealistic view of what their house is worth. When they throw out a number, it almost kills the deal before it even starts, as you are so far below them that for them to come down to your price would not only be a huge financial hit, but it would also be a huge hit to the ego. And 2) The funny way the human brain works.

Anchoring
Nobel prize laureate Daniel Kahneman in his absolutely fascinating book *Thinking Fast and Slow* tells about a very interesting test he conducted that provides great insights to negotiating:

…we told participants in the Exploratorium study about environmental damage caused by oil tankers in the Pacific Ocean and asked about their willingness to make an annual contribution 'to save 50,000 offshore Pacific Coast seabirds from small offshore oil spills, until ways are found to prevent spills or require tanker owners to pay for the operation.'

This question requires intensity matching: the respondents are asked, in effect, to find the dollar amount of a contribution that matches the intensity of their feelings about the plight of the seabirds. Some of the visitors were first asked an anchoring question, such as "Would you be willing to pay $5…" before the point-blank question of how much they would contribute.

When no anchor was mentioned, the visitors at the Exploratorium—generally an environmentally sensitive crowd—said they were willing to pay $64, on average. When the anchoring amount was only $5, contributions averaged $20. When the anchor was a rather extravagant $400, the willingness to pay rose to an average of $143. (pg. 124-5)

This is the power of what psychologists call *anchoring*. Think about this example for a moment. The same types of people, randomly selected, reduced the amount they were willing to pay by 75 percent when given a low anchor and more than doubled it when given a high anchor. Indeed, some examples of the power of anchoring are almost surreal and rather disturbing. Kahneman again:

German judges with an average of more than fifteen years of experience on the bench first read a description of a woman who had been caught shoplifting, then rolled a pair of dice that were loaded so every roll resulted in either a 3 or a 9. As soon as the dice came to a stop, the judges were asked whether they would sentence the woman to a term in prison greater or lesser, in months, than the number showing on the dice. Finally, the judges were instructed to specify the exact prison sentence they would give the shoplifter. On average those who had rolled a 9 said they would sentence her to 8 months; those who rolled a 3 said they would sentence her to 5 months. (pg. 125-126)

Kahneman provides an in-depth explanation for this psychological phenomenon, but in brief, anchors trigger our more automatic thinking processes (System 1), such as recognizing familiar symbols or faces. System 1 then sets the plate for the more deliberate thinking processes (System 2), which operates when trying to do more difficult tasks such as arithmetic or abstract thought.

As we all know, System 2 is lazy and likes its job made easy. So, System 1 obliges. Anchoring feeds System 1 something to hang onto, which proliferates up to System 2 and influences the rational mind when it comes time to buckle down and do some serious thinking. In other words, making the first offer sets the ballpark for negotiation.

Real Estate Negotiations

An effective tool I've found when negotiating with sellers (particularly those who have an inflated view of their home's worth) is to make my case first before either of us has had a chance to throw out an offer.

So, let's say I just recently bought a similar house nearby, or better yet, more than one. I describe those purchases to the seller to explain how I'm deriving my valuation. I could discuss the defects of the house that will require rehab and an estimate for that. And also bring up nearby comps or anything else that supports my offer.

I'm not a flipper, but I do explain that we only buy deals we could flip. Therefore, you can just lay out the whole process. If it needs repair, explain that it's most likely investors will be the only ones interested. Describe to them the 70 percent Rule, or better yet, break out the expenses individually and show them what it will take to make the deal work for you. Then make the offer.

All of this will dissolve the delusions of grandeur many sellers are af--flicted with, while simultaneously anchoring a realistic and profitable price for yourself in their mind.

But please note, while negotiating is an important skill to learn, it's important to not use these tactics unethically or to become some sort of used car salesman-type. The goal is to dissuade overly optimistic sellers and provide a service by being able to purchase a motivated seller's house quickly and easily at a price that will be profitable, not to trick someone. If that's the goal, you will gain a bad reputation, and deals may very well blow up in escrow as the seller starts to believe they are getting screwed and desperately tries to get out of it.

If You Are on the Receiving End

So let's say you get beaten to the punch, and the other party makes the first offer. Kanheman describes the approach of psychologists Adam Galinsky and Thomas Mussweiler when someone makes an opening offer that is too high: "*They instructed negotiators to focus their attention and search their memory for arguments against the anchor"* (Pg. 126-127).

If you are conscious of the anchoring effect, you can counteract its influence and bring yourself back to a neutral state. System 2 needs to actively fight off the unsolicited influence of System 1. The worst thing to do is get so caught up in the negotiation (and the anchor) that you buy or sell something at a price you shouldn't have.

As for Kanheman… well, I will end with his rather colorful advice: *My advice to students when I taught negotiations was that if you think the other side has made an outrageous proposal, you should not come back with an equally outrageous counteroffer, creating a gap that will be difficult to bridge in further negotiations. Instead you should make a scene, storm out or threaten to do so, and make it clear—to yourself as well as the other side—that you will not continue the negotiation with that number on the table.* (Pg, 126)

In other words, use the patented "Toddler Tantrum" method of negotiating.

Don’t leave money on the table: Strike Price vs. Goal Price

There is no question that having a strike price is an invaluable tool not only when it comes to real estate investing, but with any sort of large purchase. After all, there’s a reason auctioneers talk so fast. As *Slate* pointed out, the speed is “intended to give the buyers a sense of urgency: bid now or lose out.” But as any decent real estate investor knows, not buying a deal does not mean you “lose out.”

Having a strike price (a price that’s the highest you’re willing to pay) ahead of time is what prevents us from getting carried away in the competition of an auction or negotiation. It prevents us from confusing buying a property with winning. Oftentimes, buying a property means you lose. So never go into a real estate negotiation without a strike price.

But that being said, there is a downside to the strike price. It can subconsciously become the goal to aim for that could prevent you from doing even better.

Aiming for the Strike Price

Not too long ago, I (Andrew) was trying to negotiate the purchase of an apartment and had done pretty well up front. I had met the seller at the property and asked all the questions I needed to know in order to make an educated decision. I had spent two hours there, just talking with the seller and building rapport. I had also collected all the necessary documents, such as the profit and loss statement and rent roll.

I then went back and crunched the numbers. I came up with an offer price and a strike price. It looked like this:

List Price: $795,000 **Offer Price:** $690,000 **Strike Price:** $725,000

I still had a few questions to answer, and I figured the best way to do this would be to go over the deal face-to-face (especially since there was no agent involved). Face-to-face negotiations are usually the best, as they allow you to tailor your approach to the individual seller instead of just being another justification-lacking offer, bound to get lost in the netherworld of someone's email inbox.

So, I invited the seller to our office, and we again talked for about an hour before negotiating anything (he's a bit of a talker if you haven't figured that out yet). I then went over my questions to make sure my assumptions still held. Then I made my case: I explained that I took his numbers from 2014, then plugged in a few more (such as a management fee) and also increased a few things (such as utilities because the property would operate at a higher occupancy and some of the utilities are paid for by the owner). I then said we needed to hit a certain cap rate, and that would put us at $690,000.

He responded by saying that was way too low. I didn't flinch. Instead, I leaned forward and asked, "So at what price would you be willing to sign a contract today?" Then I paused.

So far I had done pretty well. You can argue that I should have asked for a reduction before making my offer, but I think it's often better to justify your price first. It's a process called "framing," which works similarly to anchoring, or setting the ballpark of the negotiation.

Either way, I then made a mistake. He came back at $740,000. That's a substantial drop. But instead of thinking "What's the best deal I can get?" I had the strike price stuck in mind. I came up all the way to $715,000, thinking (or maybe not thinking) we could meet in the middle at $725,000. In my defense, I knew as soon as the words left my mouth that I had come up too much. But the reason I came up wasn't temporary insanity or bad negotiating skills (well, that's debatable), but simply that I had that strike price stuck in my mind as *the* goal.

What I should have done is pause again. Go back to my analysis and explain why it would be tough to go over $700,000. Maybe he would come down a little more before I even countered. If not, I could come back at "an even $700,000" or something like that. Maybe I could get him down to $715,000 or $710,000. Instead, I left money on the table of the sacred strike price.

Aiming for the Goal Price

Now, that's not to say this negotiation was a disaster. We went under contract at the price I wanted to get the property for: $725,000. However, upon reflection, I knew that I had not only done something wrong, but was also going about things wrong in a structural way. I was putting way too much emphasis on the strike price. Remember what a strike price is; it's the highest price you're *willing* to pay for a property. What it is not is the price you *want* to pay for the property.

So I've added a number. I still have an offer price and a strike price, but I also have a *goal price*.

The goal price is the price I really want to get the property for. In other words, the goal price is what you're aiming for and the strike price is what you will settle for. Looking at it this way can even make you reconsider your offer price. "*Am I leaving too much on the table?*"

After all, had I offered $675,000, the seller probably would have still come back at $740,000, maybe even a little less since I anchored the price lower. You want to find the lowest offer price that isn't so low as to offend the seller. I doubt an extra $15,000 would have done that.

So if I had another chance at the above situation, I would have probably come up with the following:

List Price: $795,000 **Offer Price:** $690,000 **Goal Price:** $700,000

Strike Price: $725,000

Would it have worked out better? There's no way to know. But what I can say with a lot of confidence is that the strike price should not be something to aim for; it should be something to settle for. You should always try to do better. Our subconscious minds will aim for the price you set ahead of time. So why not set a lower price to aim for and if you can't get there, then settle for the strike price? That way, you won't let your subconscious mind leave money on the table.

CHAPTER 7

THE REHAB VALUE-ADD

BRRRR: **B**uy—**R**ehab—**R**ent—**R**efinance—**R**epeat

➢ **2nd BASE**

—Renovation

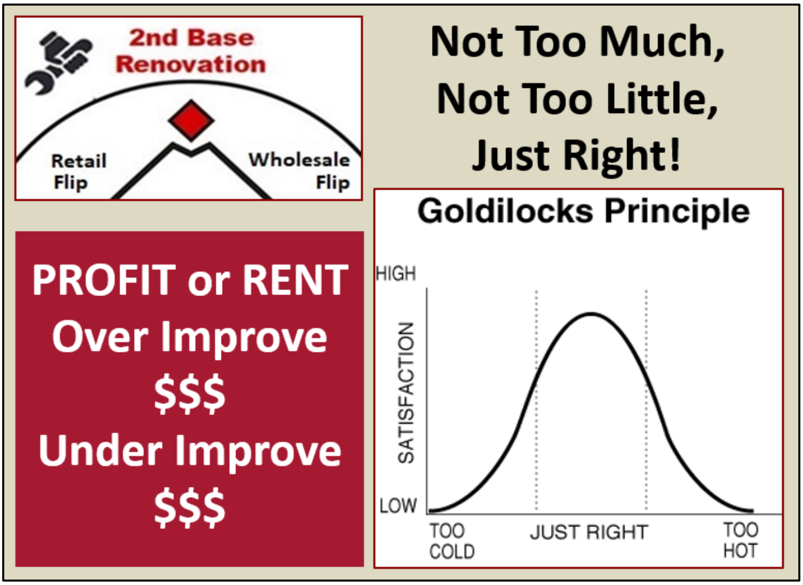
There are numerous ways to add value, but the general means of adding value is through upgrading the physical appearance and functionality of a property. Often the reason we are getting a good deal in the first place is because the seller has a problem (remember, we are real estate problem solvers). Often that problem is that the property is not in the best of shape or is outdated, and he can't or doesn't want to go through the necessary effort or expense to get it ready for a Realtor to show it to the general, retail buying public. So, the seller is open, or at least should be open, to a wholesale price.

A quality rehab can provide us the profit edge or equity potential we need. BUT it is easy to rehab the profit/equity right out of a property if we're not careful. There is a nearly universal tendency to underestimate rehab costs by sellers, agents, and investors. I don't think I've met an investor who hasn't done so, and, sometimes, extremely so.

Construction and holding costs often abide by Murphy's Law: what can go wrong will. So, we must build in a healthy margin into our offer after determining a realistic scope of work and rehab budget. Being liberal with our budget numbers helps us be more conservative with our offers! When it comes to expectations for contractors, we face a daunting equation. At best you get two out of three—quality, speed, price—but not all three. How you balance your expectations with your desired outcome will test your metal as a rehab manager.

Developing a team of trusted and skilled field staff/contractors is a critical part of getting the most for our rehab dollar. Our operation depends on how efficiently these teams are managed for speed, and quality. Every extra day on the job equates to hundreds of dollars flying out the door. A few days less can mean all the difference between the success and failure of meeting budget goals. It's often the small finishing details that contractors would like to leave for their next job but don't write that last check until they're done!

There's a little science and a little art to figuring out the optimal level to upgrade a property. We're looking to hit the "Goldilocks Rehab Zone"–not too much or too little, but just right. Flipping requires the house to shine, while holding necessitates that it looks agreeable and is functional. This is a key distinction.



The aim for rentals should be for durability and functionality first, style second. That said, there is nothing better than curb appeal to act like a welcome mat to both potential buyers and renters. Knowing our end user and catering our upgrades to them will make the difference in getting the best sales or the highest rents.

It's critical for our sanity and efficiency to find pleasant and consistent design features and standardize them throughout: two-color paint, countertops, flooring, bath fixtures, etc. used for each one of our projects with some quality distinctions depending on the property.

This goes a long way to standardizing our cookie cutter process. (We even have three consistent exterior color schemes and a standard color for doors.) Anything we can do to lower the number of design decisions we have to make for each job saves time, energy and money.

It's too easy to move on to the next project without evaluating the last one. But the best way to improve is through such an assessment:

- Did we hit our budget? What were the successes or setbacks?
- Which field staff/contractors met or exceeded expectations?
- What could have been done better to hone down costs?
- What was learned to make the next job better/more profitable?
- What systems are we putting in place for better efficiencies?

With apartments and other commercial real estate, it's especially common to talk about a "value add," a "value play" or "repositioning" a property. These are improvements that you can add to a property to increase the property's value more than the cost of the improvement for rent increases.

Adding Value to Your Rentals

1. Adding a Bedroom

Families want at least three bedrooms so if there is enough square footage, try to make a two bedroom into a three. People also like a larger master bedroom. So, if you have four small rooms, consider taking down a wall to make for a larger master bedroom space.

You must ask yourself, what are you willing to sacrifice and at what cost? The best situation is when there is a bonus room that can be converted even if it is on the small side. Some older houses have such large living rooms that you can carve out an extra room there.

2. Garage Conversions

Residents like their garages, but there may be situations that it would be better to convert them into bedroom space. These can look awkward, but you'll have to determine what change (and at what cost) would demand more rent.

3. Finishing Basements and Attics

Many appraisals won't even count bedrooms, bathrooms, or square footage in finished basements (even walkouts). To consider finishing a basement the following things must be true:

1) The neighborhood is strong, warranting such expenditures.
2) The additional amount of rent generated from the increased square footage and usage makes it worthwhile to do.
3) It is a walkout basement (one side is above ground, one is not) with easy egress. For example, the photo to the left is in a finished "basement" with the other side of the house below grade.

And one more quick note. Even if a basement is not a walkout but is orderly and has a ceiling (preferably), painting the walls white and the floor grey makes it come to life as a semi-finished basement at a cheap cost as the above photo to the right shows.

4. Making a Half Bath Whole and Adding Bathrooms

Some half bathrooms are small, and there's just nothing you can do. But if there is extra space, it can be a good idea to put in a tub/shower.

As far as adding a full bathroom, unless it is a huge house, I would only consider it if the house had only one bathroom. Other than that, it really depends on the value of the house and whether there is space for it. In lower end neighborhoods, it would generally not make sense. But in higher end neighborhoods it very well might. This is especially true if there is a genuine master bedroom that lacks a master bath. In such cases, the return may outweigh the cost.

5. Adding Storage

If a house has neither a garage nor a basement, it is probably a good idea to add a shed in the backyard. People like their stuff and need some storage for it. Look to Home Depot or Lowes for such a shed.

6. Opening up the Kitchen

There is nothing that sells or rents a house like a nice kitchen. A confined, closed-off kitchen simply won't do. Here's an example of one such god-awful kitchen that we were able to dramatically rearrange:

Sometimes, however, there's no good way to add space to a kitchen. You may, however, still be able to make it feel open by opening up a wall to the living or dining room. It could be as simple as cutting a large opening in a wall. Here is an example of the difference that opening a wall can make and another example of adding a bar.

7. Improving the Aesthetics (Particularly the Front)

Never underestimate the power of aesthetics. Even small things can make a difference. Compare the following photos of small changes.


There are many fixes that add far more value than they cost such as:


- Grass, plants and mulch
- Pavers
- Repair fences, front, and trim
- Power washing
- Shutters, window boxes
- Awning for the windows or remove
- Remove satellite dishes on the roof and weeds in the driveway
- Paint the front door
- Replace ugly mailbox, light fixtures, address
- Hedge the trees and bushes and mow the lawn
- By the way, these photos show how a slight angle shows better.

There are certainly other ways to add value, including more drastic measures, such as mother-in-law quarters, turning the house into a duplex, adding an addition, etc. But for the most part, the above ideas can add substantial value to any flip or rental, and you should be at the ready to use them when the time comes. If the project adds more value than it costs, it should be considered. Not only will it add to a property's salability but also, it's rentability. And if renters like the place they are living it is likely they will stay there longer.

All of this applies to turnovers as well as rehabs because when renters leave you often have the need or opportunity and expense to upgrade.

Create Your Scope of Work

Over my years, I (Andrew) have seen many times when someone will hire a contractor to do a job where the final scope looks something like this:

- Exterior (repair fence, rot, shutters, landscaping): $2,400
- Interior (paint, replace windows, replace doors, etc.): $4,300
- Kitchen (cabinets, appliances, countertop, flooring): $5,900
- Bathroom (toilet, shower surround, vanity, door stop, toilet paper holder, towel rod, soap holder): $5,200
- Bedrooms (build closet in left bed, flooring, etc.): $3,500
- **Total Price: $22,400**

And that's about it. Forget the numbers and items on that above "scope," as they're just there as an example. Generally, my experience with such bids is that a lot of knick-knack work will be left undone. There will generally be confusion as to what was agreed to, particularly in terms of what type of materials are to be used, the smaller items, and sometimes even the location.

A friend of mine hired one contractor and told him to put the laundry hookups on the first floor, but he instead put them in the basement despite the verbal agreement. Unfortunately, it wasn't in the scope, so there wasn't much that could be done after the fact except argue about it.

Furthermore, costs can be hidden in those paragraphs of things they will do. If you'll notice above, I put a lot of stuff under the "bathroom" category, but most of them were petty items (towel rod, toilet paper holder, door stop, soap holder). Unless you are putting in a diamond-encrusted toilet or a solid gold shower surround, there is no way that should cost $5,200. But it's harder to spot these sorts of things when a contractor is quoting multiple items at a time.

This is why demanding individual line items is so important:

1. It's much easier to spot things that are overpriced. You can also bid things you are on the fence about and see whether the price makes it worth it to do or not.
2. It's easier to compare one contractor's bid to another since you know they are bidding the same thing.
3. It reduces miscommunications, and you can make sure the contractor is bidding all of the work you want done.

So how do you put together a scope of work? We'll start with your first walk through, before you get the property under contract:.

Initial Estimate

For this, I highly recommend J. Scott's book *The Book on Estimating Rehab Costs*. He lays out 25 different categories that will induce expenses. I added a few (for example, I separated basement and foundation) to make my initial estimate. The Items are as follows:

- Roof
- Gutters/Soffits/Fascia
- Siding
- Ext. Paint
- Decks/Porches
- Concrete
- Garage
- Landscaping
- Septic System
- Interior Paint
- Carpentry/Framing
- Sheetrock
- Flooring (HW/Carpet)
- Flooring (Vinyl/Tile)
- Bedrooms
- Bathrooms
- Cabinets/Countertops
- Appliances
- Windows
- Insulation
- Basement
- Foundation
- Demo
- Plumbing
- Electrical
- HVAC
- Permits
- Mold
- Termites/Pests
- Other

I put together a one-page form that allows me to quickly estimate the rehab costs. First, I note the basics about the house (i.e., the ARV, asking price, beds, baths, garage, neighborhood quality, etc.) and then put together an estimate on each of these items. I add for extra knick knacks, a sewer line contingency (if the house is older), estimated holding costs, and general contingency (usually 20%). Then I add them up for my total estimate. Here is what it looks like:

Property Analysis Sheet

Address				List Price	Offer	Goal Price	Strike Price
Bed	Bath	Approx Sq. Ft.	Seller	Rehab Estimate		Rent Estimate	
Garage/Carport	Basement	Neighborhood		Est. Value	Age	School	
0 / C / 1 / 2	F / WO / Y / CS / N	A / B / C / D +/-					

Location

Roof		
Gutters/Soffits/Fascia		
Siding Type:_______		
Ext. Paint		
Decks/Porches Deck: Y/N		
Concrete		
Garage		
Landscaping Tree Trim: Y / N		
Septic System Septic: Y / N / M		
Interior Paint		
Carpentry/Framing		
Sheetrock		
Flooring (HW/Ca HW / Carpet / Mix		
Flooring (Vinyl/T Vinyl / Tile / Mix		
Bedrooms		
Bathrooms		
Cabinets/Countertops		
Appliances Replace: Y / N		
Windows Type:_______		
Insulation In walls: Y / N / M		
Basement		
Foundation Evaluate w/Pro: Y / N		
Demo		
Plumbing Pex / Copper / Galv		
Electrical Panel / Push / Fuse		
HVAC Central A/C: Y / N		
Permits Need; Y / N		
Mold Present: Y / N / M		
Termites Present: Y / N / M		
Other		

Condition Notes		
	Knick Knacks	
	Sewer Line Cont.	
	Holding Costs	
	Project Cont. (20%)	
To Investigate:	Total Estimate	

So, for example, if all the line items added to $20,000, the final part of the scope would look like this:

- Rehab Estimate: $20,000
- Knick Knacks: $1,000
- Sewer Line Contingency: $500
- Holding Costs: $2,500
- Project Contingency (20% of rehab estimate): $4,000
- **Total Rehab Estimate: $28,000**

Of course, you might be better than me at estimating up front and not need to add the contingency. From experience, I've found that unforeseen items and things I missed usually add up to about that, so this is what works for me. You will need to customize it somewhat.

As far as how to estimate expenses, it depends on what materials you are using, what quality contractor you are using, and sometimes, where you live. I recommend analyzing the quotes you've gotten from contractors, asking contractors and other real estate investors in your area, and analyzing the prices of various things where you live. This is something you will definitely want to learn.

By being able to put this estimate together quickly and on one sheet, you can make your offers with confidence that you won't rehab out all of your equity. But this alone isn't something you can send to a contractor for a bid. For that, we need to put together a scope of work: *How to Accurately Estimate Expenses on a Rental Property in 3 Steps*

Scope of Work
With scopes of work, you look to catch every little item. For this reason, you really want to make sure the utilities are on. Sometimes that will require doing work up front, and it's usually better to get that done and then do the scope of work afterwards.

We have a large checklist that's six pages long and go through each room in the house to mark off and make notes about each item in each room. Yes, this is a tedious process, but you want to be thorough up front to avoid headaches on the back end. The front page of our scope of work template looks like this:

Scope of Work / Systems Check		Test
Address:		Electricity
Date:		Gas
Done by:		Water

Due Date:	Stage: Clean----Turnover----Rehab
	Total Estimate:

Lot	X	✓	#	Comments:
Landscaping				
Tree Trimming				
Grading				
Driveway				
Walkway				
Rail				
Fence				
Gate				
Deck				

Exterior	X	✓	#	Comments:
Paint				
Siding				
Roof				
Vents/Chimney				
Gutters				
*Downspouts				
*Splashblocks				
Window Trim				
Address Numbers				
Mailbox				
Water Spicket				
Front Porch				
Deck/Patio				
Soffits				
Fascia				
Rim Joist				
Storm Door				

Other Exterior	Comments:

I’ve known people who just bring in a notepad and start making notes. But I find the checklist to be more helpful, as I’m less likely to miss something. (On an aside, this is true for almost everything. For more, read *The Checklist Manifesto: How to Get Things Right*.)

As you can see, on the right, there is a space for extra items that aren’t listed in the checklist. Your scope of work system doesn’t need to look like mine, but it should be very thorough and detailed. Don’t rush through this process. It takes us between 30 minutes to as much as two hours to fill one of these out, depending on the size of the apartment unit or house and how much needs to be done.

We then transcribe this into a scope of work template. It would be nice to bypass this phase, and if you can write up a scope with an iPad on site, more power to you. But I type slowly on iPads/laptops, and it's too hard to get everything in the right order, so we use a two-step process. The final product looks like this:

		Status	Scope	Bid 1
2			Bid #1	
3			**512 NW Ward Ln**	
4				
5			Prework	
6			Turn on water + test	25
7				
8			Lot	
9			Clean out debris in driveway	10
10			Remove Basketball Hoop	25
11			Kill weeds in driveway and walkway	10
12			Add bark mulch in flower beds	75
13			Add bark mulch in backyard	75
14			Take out tall plants in back flower bed	10
15			Repair fence on right	200
16			Remove debris in backyard	25
17			Cut + Cap BBQ in backyard	35
18			Remove lawn mowers and other stuff	20
19			Remove wood on left and any stone in back right (not around flower bed)	15
20			Rake off patio in back	15
21			Exterior	
22			Wash house	25
23			Remove flag	15
24			Remove duct tape on front	1
25			Clean debris off roof	20
26			Clean out gutters	35
27			Reattach left elbow of downspout	10
28			Add address numbers	20
29			Add mailbox (black)	50
30			Add water spicket by garage	100

We separate each item out into four sections:

- ***Pre-Construction:*** This means things like fixing the electrical so the power can be turned on, which is usually done before the scope is put together.
- ***Construction***
- ***Vendor Items:*** This includes anything we don't have our main contractor or construction crew do. It might include things like painting, flooring, appliances, foundation repair, tree trimming, etc. If your main contractor is doing everything, this list is unnecessary.
- ***Punchout:*** These are the last items that need to be done after the painting and flooring. It includes things like outlet covers, door stops, installing the appliances, cleaning the carpets, and general cleaning.

We use a software program called Smartsheet and after the scope is done, we send it out to any contractor that is going to be bidding the project. We also create a budget up front to make sure the quotes are in line with what we are thinking. (This is also good practice when it comes to determining how much rehabs will cost.)

We also require they put the bid into that template. Early on, it may be hard to demand this of a contractor you've just met, but you should request it. It is much easier to compare different quotes if they are on the same template. The vast majority of contractors we've met have had no problem with doing this. After a project is accepted, we also ask contractors to put any add-on requests at the bottom of the page.

If you use employees on your staff to do your rehab projects, make sure to track them after the fact so you can see if their costs are in line with your expectations. If your system is working well, they should be saving you money, as much as 20-25%, over what contractors are costing you, but you won't really know unless you actually track it.

The Bottom Line is the Bottom Line

Regardless of whether you want to use a system like ours or one quite different for putting together scopes of work, it is very important to be thorough and consistent about it. A messy scope of work will lead to a messy project. And a messy budget will lead to a blown budget. ”Give me six hours to chop down a tree,” said Abraham Lincoln, “and I will spend the first four sharpening the axe.” Do the leg work upfront, and the project, will likely go much more efficiently and smoothly.

Factor in the F.A.R.E. Future Anticipated Rehab Expenses

One way, maybe the primary way, we underestimate rehab is not to factor in what future expenses await us, especially if we purchase a property that with a renter living there. In such situations we need to give the property a FARE number: the anticipate expenses it will take us to rehab that property once the resident leaves. Don't let the FARE lay in wait as an nasty surprise. Factor it in from the start!

Finding the Right Contractors

Okay, when it comes to work from contractors, you can have two-out-of-three but not all three: 1) price, 2) quality or 3) speed. You choose.

And, of course, sometimes you only get one…or none. Ugh! A lousy handyman or contractor will cost you money, time and frustration to say the least. So, how can you find a solid contractor, maybe even one who teams up with your company for years, even decades to come?

Start with referrals
If someone has done good work before they will likely continue. So, piggyback on someone else's real-world experience. A good carpenter will likely know a good plumber and a good HVAC contractor will likely know a good electrician. Ask family and friends along with investors and real estate agents. Start before you need them and keep a list.

Go to places contractors go to
When looking for quality plumbers, go to plumbing stores and ask. Same with electricians, painters, carpenters, etc. Park out at the nearest Home Depot or Lowes store at 6:00 am to see who shows up early. It is often diligent contractors wanting to get an early start on their day—the ones you want!

Place Craigslist Ads
Not only can find those advertising their services there but you can post wanted ads looking for local handymen or contractors in the category where they place their ads.

Screen your potential candidates
Beside referrals find contractors by stopping at job sites and writing down phone numbers off of work trucks. But either way, screening is the next critical step, first on the phone then in person.

What's your initial impression? How long have they been in this line of work? What does their truck look like? How many employees do they have? How much do they oversee their projects? What are their best skills? What is their workload right now? When can they start?

Ask for references

Get phone numbers of who they have worked for and make sure you call them with specific questions regarding their work performance and whether expectations were meant: Did they have any problems? Would they hire them again? So we go on "gut instinct" and do not take the time to call references. This is about as smart as not calling a prospective renter's prior landlord. And finally, when possible, visit a place they've rehabbed to check out their work first-hand.

Google the name of the contractor

Look them up on Yelp, BBB, Home Advisor and Angie's List. You are especially looking for the worst reviews so when searching them include the words "scam," "court," "sue" and "rip off." Of course, not all complaints are appropriate, but they do offer a "red flag" that be investigated further.

Don't cut corners

To keep a lid on expenses, we often use contractors who lower professionally than those reviewed in Angie's List. This is understandable but don't build your business on paying people under the table.

Not does paying under the table promote an unethical environment, the first accident they have without workman's comp could lead to you ultimately paying for their injuries and sink your company. Know the difference between a contractor and an employee as defined by the Dept. of Labor in your state and abide by this distinction.

Verify their license

You'll need this information at the end of the year for tax purposes so why not get it upfront and check out that "they are who they say they are" when it comes to being licensed. Verify too that they have the correct insurance needed to protect themselves and you.

Meet them on the jobsite
Are they on time? Are they early or late? How do they carry themselves? Do they seem to know what they're talking about? Do you sense that they tend to over promise and under deliver?

Check them out on a smaller task
Before hiring them for a large rehab, have them complete a smaller task. Does their work come in on time, on budget and with the quality you were expecting? "He who is faithful in small things, is given more!"

Make them compete whether they know it or not
You do not want to be dependent on one contractor even if they're good. Life happens and contractors get distracted with other jobs. You don't want them to get complacent with your business or you may find yourself being taken advantage. Competition drives quality, price and speed and you want them to know that you have other options.

Always be clear about your expectations
A lot of rehabs go sideways because of unclear expectations which often starts with a bid that does not specify items to be completed, including punch out and clean up. The more detailed you are upfront, the less likely you'll be unsatisfied with the final product.

Weigh out price versus cost
Price is what you pay for something now, but cost is what you pay for something long-term. You don't want to be so fixated on the cheapest alternative that you spend a lot more in the long run.

Someone needs to be the project manager
At first that someone is likely you. Later you may hire or elevate a person who works for you as project manager. There is a lot to be said for showing up to the jobsite on a very regular basis to check out progress and to clarify any questions so that the work goes smoothly. And please, after the initial draw, never pay for what is not completed!

Building Out a Team of Employees Rehabbers (vs. Contractors)

Many of our Stewardship's partnership businesses have developed a skilled team of employee laborers and skilled workers, alongside of key contractors. Such teams have disadvantages and advantages.

The disadvantage is that such employees generally work by the hour instead of the bid and thus have less incentive to move quickly and efficiently. Time for a contractor affects their money while time for an employee, affects your money. We've have had employees, for example, quit for the day with a half hour left of work on a jobsite. A contractor would never do that, realizing the extra driving and set up time makes no sense to their bottom line. We've also seen when there are way too many trips to Home Depot or two going at a time.

But there are advantages as well. Employees are yours to go when and where you need them at a moment's notice. They can more easily "tag team" on projects with lower skilled guys pulling carpet and prepping for rehab before higher skilled guys get there.

Also, we've seen many guys come in as laborers who, over time and under the mentorship of our older guys/gals (including contractors who work for us fulltime), have developed a significant amount of skills to tackle increasingly more complicated work. We've even seen laborers come in, become team leaders and later partners. That's a thing of beauty!

Likely, when you are just starting off you will primarily use contractors but keep your eyes open for who you could hire for maintenance as well as for turnovers and rehabs. You (or better yet, your project manager) need to have a commitment to build a great culture (like what you want to have with your office staff) that breeds trust and pride. (Often, by the way, this includes having a shop.) If you do create such a culture, not only can you save money, but you will create a powerhouse team that will help you take on more lucrative projects.

CHAPTER 8
QUALITY PROPERTY MANAGEMENT (KEEPS YOU) RICH

BRRRR: **B**uy—**R**ehab—**R**ent—**R**efinance—**R**epeat

➢ **3rd BASE**
—Management

While it's true that we make our money when we buy, it's also true that we won't see that money until we sell or rent. Now it's time to extract value from our hard work of acquisition and rehab.

Habit #2 in Stephen Covey's helpful book, *The 7 Habits of Highly Effective People* applies here, "Begin with the end in mind." The purpose of flipping properties is the sale, pure and simple. Flippers seek to build a system that creates as much profit as possible.

Wholesale flipping to other investors focuses on thinner profit margins and higher volume. Wholesale flippers seek to build a buyer's list of investors who will be repeat buyers. Retail flipping to homeowners focuses on marketing to one-time buyers through your own efforts or those of a key Realtor you regularly use.

Buy and hold investors have the long-term task of creating high-quality property management. This includes a thorough understanding of your state's *Tenant and Landlord Act*. As such a business grows, so must its infrastructure to support marketing, accounting, leasing, paperwork, maintenance, turnovers, etc.

Over a few generations of staff, our company in Eugene became very good at property management for student housing. Many of our first office staff were, in fact, students themselves or fresh out of college. We learned to track the campus schedule closely and time our leasing accordingly. We figured out that it was much better to lease to a group as opposed to individuals in a house and that having a volunteer "house manager" helped streamline maintenance requests. Realizing that students would not have the needed income to qualify for a place on their own necessitated the (wonderful!) opportunity to have parents co-sign for virtually every student resident.

When our company expanded to the Midwest 2011 and focused on working-class and lower middle-class areas. In Kansas City we brought our college property management mindset along with us…until we started losing money. We had failed to begin with the end in mind.

Obviously, our parental co-signers model didn't apply anymore, but it still took us quite a while to realize that more stringent criteria needed to be applied to qualify would-be residents. While we had almost never evicted a college student, we were finding ourselves at the eviction courts in Kansas City on an agonizingly regular basis.

Eventually, we determined that we weren't going to be "second-chance landlords." Instead, we implemented a policy where we would only rent to people with no evictions on their record except in very rare cases. This, along with a number of other such criteria, eventually turned our money losing management enterprise around.

It is possible to avoid involvement in property management altogether and hire it out to a third-party firm. A case could be made for such outsourcing if it allows you to focus on other, money making aspects of real estate investment or if you are out of state. We are, however, not fans of outsourcing property management unless it is to a partner, because we see property management as foundational to building a large real estate investment business.

Critical Principles of Property Management

1. Screen, Screen and Then Screen Some More

Who you let into your rentals is the most important decision you make as a landlord. It is better to keep a property vacant than to let someone in who will stop paying and force you to evict them, trash the unit or just be a never-ending pain. If you were going to lend out your car, would you lend it to just anyone? Or would you only let someone you can trust borrow it? A rental house is usually worth a lot more than a car. So, you should be extra careful of who you let in.

We would recommend not letting anyone in with an eviction unless it's quite old (at least five years, preferably ten) and has been paid off. Do not approve violent or recent felony convictions. They should also get a good landlord and employment reference and make at least three times the rent in income.

We have used a resident screening company with solid success. This way, we (and you) aren't tempted to hear what you want to hear when you call landlords and employers for references. However, if you do call the references yourself and hear a landlord say something like, "Well, if you don't mind [something bad], he should be a good tenant," then it's time to run the other way!

In general, here is our screening criteria:

- No evictions in the last 10 years
- No more than one eviction
- No felonies (other than one DUI) in the last 10 years
- No violent felonies
- Three times the rent in income
- No more than one late pay per year in their rental history
- No bankruptcies
- A credit score at least above 500, and unless everything else is good, above 600

The quality of your renters determines the quality of your returns.

-G. Brian Davis

You can rent based on this quote from the "get-go," or you can ignore it and experience the consequences of your disregard after the fact!

Screening is a bit more complicated than just applying the above criteria because the issues intersect and have nuance. But the criterion needs to be identical for each applicant. Never treat two applicants differently, or you may shortly be hearing from Fair Housing.

2. Understand: Your Prospective Residents Will Mirror Your Rental
If you are trying to rent a dumpy unit, you can guess what kind of resident you are going to find. I'm not just referring to areas. Yes, it is harder to find good residents with clean backgrounds in rough areas. However, we have several properties in rough areas, and we have found plenty of good residents for them. You just have to screen more and likely say "no" more.

But if you try to rent a house with ripped vinyl, splattered paint, '80s appliances, unkempt lawns and broken window screens, the only prospective residents you are going to find are those who are desperate for a place and are willing to live pretty much anywhere.
And you can guess how they will treat your unit and whether they will consistently pay rent.

You pay for what you get. It holds true for real estate. If you put a good product on the market, good residents will want to rent from you. And trust me, as a buy and hold investor, this is what you want.

3. Be Fair, But Firm
You need to have policies and procedures in place for two reasons: 1) It will hold you accountable to not let in a bad renter if a property sits vacant and 2) It will keep you in compliance with fair housing.
But you also should have policies in place for after a resident moves in included in the lease and "taught" to residents when you sign the it with them. The lease signing should not be a short process; you need to go over each rule you have with them in detail.

So what's your policy for late rent? Well for us, rent is due on the 1st and late on the 5th. If rent is paid later than the 4th, then a late fee applies. We don't waive this unless they prove that the rent was sent beforehand, but for some reason wasn't received (say, lost in the mail). If they argue with you, just respond, "I'm sorry, but it's our policy, as stated in the lease. If I made an exception for you, I would legally have to make an exception for everyone. Unfortunately, I have to charge the late fee."

If it hasn't been paid by the 12th, we file a 72-hour notice. Then we file for eviction on the 15th. If they contact us, we will set up a one-time payment plan, but if they don't stay true to that plan, we file for eviction. Don't be the type of landlord who constantly falls for the endless stream of resident sob stories. Just blame the policy. But of course, first, you must make said policies.

4. Maintenance is the Best Form of Resident Retention

If you want to keep your residents for the long-term, do the maintenance right. Maintenance is the one thing that you will consistently provide your residents during the course of their stay. Otherwise, you're just the person that they have to pay money to each month. Maintenance is how you make them want to stay.

Don't let maintenance be an afterthought. Get to urgent issues immediately and get to the other ones timely. Make sure if you can't afford to have a maintenance guy on staff that you have someone at your call to do the work. Build a relationship with a plumber, roto-rooter company, electrician and HVAC technician. And find at least one handyman willing to take late-night emergency calls.

Most things aren't emergencies (even if renters think they are). Most emergencies involve water in some way or another. So, you need to have someone who can go and stop a leak at midnight, not letting the damage worsen. Or if not, you need to be able to do it yourself.
Finally, this doesn't mean you should bow to every renter's demand. It also doesn't mean you shouldn't charge residents for the damage they do. But you do need to provide good maintenance if you want your residents to stay and pay.

5. Be on the Resident's Side

Always be on the resident's side. You're the good guy. Now, there is a bad guy, too. It may be the lease, the law, the owner or the policy, but you are never the bad guy.

Many residents feel like the property manager is against them and will become hostile. In response, the property manager gets defensive, and both sides dig in their heels. This us/them approach is counter-productive and just makes everyone upset with each other. Instead, approach the problem as the resident's ally. Don't lie but explain the problem by framing it as you and the resident versus the bad guy (whatever that may be). So, let's say they are late on their rent and can't pay. They want another payment plan even though they failed on the rent. Well, make the "policy" the bad guy.

"Unfortunately, the company's policy doesn't allow me to offer another payment plan. Legally, I can't break that policy for you unless I break it for everyone. However, I think we can come up with the best possible solution for your situation. It sounds like you would need at least another week to move out and a little money to do so. What I think I can do is give you one more week and $200 [cash for keys] if you leave the property clean and in good shape. Is that something you could do?" The possibilities are endless with this approach!

The more systems your property management team utilizes, the more efficient you will be. For example, keys will become the bane of your existence unless you use a master key system. We have gone to a paperless office, scanning in all our rental applications and agreements and use our websites as much as possible. Residents apply and pay online, leave maintenance requests, etc.

Buy and hold may be the ultimate way to get rich slowly, but it's not easy. Property management is a key factor in achieving your investment goals, so learn how to do it, or better yet, how to oversee someone else who knows how to do it. These five steps are, in my judgment, the most important pieces to help you on that path.

Four Types of Residents to Avoid…Like the Plague

Okay, first of all we call our "tenants," renters or residents…and this is where the rubber meets the road in terms of our attitude. Instead of calling difficult tenants, tenants (or worse), we call them residents**.**

Why? Because the term “tenant,” while legal, can also be a bit demeaning. These are our customers and clients; those who pay off our mortgages. Their rent creates wealth in an I-D-E-A-L, amazing way for us. (See p. 14.) Similarly, we don’t refer to ourselves as landLORDS!

Okay, it’s definitely fine to vent, even scream at the sky if need be when the inevitable happens. Anyone in property management long enough will have horror stories. Indeed, we’d recommend anyone getting into the business watch *Pacific Heights* just to scare you straight and remove any illusions you may have.

We’ve all heard of “the professional” that finds a way to clog you up in the legal system and live for free for months on end. One property manager told me they spent $10,000 trying to get a guy out!

My father got sued for over $9,000 because his maintenance tech threw out a bunch of stuff he thought was trash. Let me rephrase—it was all trash, but in Oregon, you must store any belongings a resident leaves behind for 30 days. And it’s hard to prove it’s all trash. Another resident graffiti his entire apartment and even including the shower.

So, let us begin down this frightening path of resident horror stories and what to do about them. First, there are, broadly speaking, four types of difficult renters, many of which overlap:

1. The Destroyers
2. The Non-Payers
3. The Pests
4. The Professional

We’ll take each one individually.

1. The Destroyers

The amount of damage one bad resident can do to a house is truly spectacular. And, it will take a long, long time (or forever) to make up for those losses with rent. We have one recent turnover that cost almost $10,000. And it’s on a 650 square foot house!

This resident treated our precious home like the Russians treated Moscow when Napoleon was on their heels. His scorched-Earth policy left little recognizable in the wake of his unprecedented destructtion. Here's a set of before and after pictures you likely won't see on any late-night infomercials.

It may be a bit hard to tell, but yes, the entire lower half of that door is missing. What's important to know about this story is that he had been accepted by a previous manager based on a lower set of criteria because he had a voucher. This is a no-no. Just because someone's rental payments are guaranteed doesn't mean you want them to live in your house. Here's the bedroom and then the bath.

This leads to the first recommendation on how to deal with these situations—namely, stop them before they start:

1. ***Don't rush on getting a renter.*** It's better to have an empty property than to rent to someone you don't want. Make sure to screen, screen, and screen some more. Be patience to find the right resident rather than one that is questionable.

2. ***Don’t stand on principle.*** Don’t get caught up in long battle to try to get the money back in collections. Just keep the deposit and send the remaining bill to collections. Renters who leave properties in conditions like these rarely have money to pay for the damages, so it’s not worth your time and energy to try and squeeze blood out of a turnip. One time a renter stole our toilet on the way out. This petty injustice may feel like it demands reprisal, but trust me, it does not. Just move on.

3. ***Evaluate each case independently.*** In this case, the house was immediately destroyed. So, we just let the resident stay there, as there wasn’t much more damage he could do. But if such a resident lives in an apartment complex or you do believe there is more damage they can do, you should try to get them out ASAP. For example, we had a resident at an apartment that was such a slob, it brought cockroaches to his neighbors. In these cases, you want to try to get the resident to leave.

4. Consult an attorney because it’s much harder to get an eviction if a resident isn’t behind on their rent. State laws differ, but it will certainly require a paper trail of notices and warnings. If you can get the person to leave voluntarily, perhaps with cash for keys, that is all the better.

2. Non-Payers

Sometimes non-payers are deadbeats, but oftentimes they are just regular people who fell behind for whatever reason. The big thing with these residents is to take emotion out of it. Create a system and stick to that and avoid falling prey to any sob stories. Repeat to yourself over and over, “I’m sorry, but it’s company policy.”

Our policy is that rent is due on the 1st and late on the 5th. Late fees are non-negotiable (other than extreme and proven circumstances). 72-hour notices go out on the 12th, and we begin the eviction on the 15th. Tenants are allowed one payment plan but must meet it entirely or the eviction will proceed.

We explain this to renters beforehand in a long lease signing and then follow through when it need be applied. So, as far as rules for these situations go:

1. ***Create a system and follow it.*** Landlords need to have a backbone. Everyone has a sob story, and they will want to make their problems yours. Don’t let it happen. And don’t just wing it. Create a written system of procedures to follow.

2. ***Screen, screen, screen.*** Okay this is the third time I’ve mentioned this! But you also pull references on prospective employees, right?!! We don’t accept evictions unless they are 20 plus years old, and even then, we’re not happy about it. Residents also need to have three times the monthly rent in income and a good landlord and employer reference.

3. The Pests

These types of residents may be either a pest to you or to their neighbors. They very well will call and complain about every little thing and want you to do all sorts of minor maintenance. This is one of the reasons we have a long lease signing. We want to hammer in every detail about what we will and won’t do as well as what we expect from them regarding our expecting including no smoking in the residence.

Such renters may want a new storm door or for you to replace the locks or whatever. Or they will want discounts for standard maintenance items. Or they will demand something be fixed immediately, perhaps even calling after hours because their sink is clogged up. As my brother says, "If a homeowner couldn't get someone to fix it any quicker, then we can't be expected to." I would recommend other managers think that way.

Some resident complaints will be legitimate, but when it goes too far and they're basically just complaining for the sake of complaining or trying to get something for free, you need to stand your ground. If you capitulate, you will only incentivize such behavior.

Other times, these residents will cause problems with neighbors. We once took over a property where one of our inherited renters had let two prostitutes stay with him. Apparently, they got into a fight around 2:00 a.m. and one was holding the other off the third story balcony while screaming at her at the top of her lungs. Fun times.

Another guy basically panhandled the other residents every day for spare change and rides. Another had a boyfriend who broke in through a window and cut himself and ended up bleeding all over the hallway. And we've had several drug dealers.

A friend of mine in the business made an astute observation. There are generally two types of these renters: 1) the ones that cause problems and 2) the ones that blend to their environment. So if the building is good, they will be good; if it is bad, they will be bad. You need to target the first group and get rid of them as quickly as legally possible. Here are the keys:

1. ***Screen like it's a broken record. Oh, it is. This is our fourth time saying it.*** Indeed, behavior is always something to look for, which is why we also don't accept violent or recent felonies and want strong landlord references.
2. ***Use psychology…*** *!*

3. ***Follow the law.*** Talk to your attorney about the procedure to follow in your state. Again, it will almost certainly require a paper trail of warnings and notices. Written complaints from other residents may be required, so be prepared to ask for these. Or if it's a month-to-month lease, just give them a 30-day no-cause notice (if your state allows that).

4. The Professionals

This monster from deep that haunts us all is the main reason we must be particularly careful to follow landlord-tenant law to the letter. These folks know how to exploit the system and are more than willing to do it. This is the *Pacific Heights* scenario. Other than screening, the key thing here is to not take things into your own hands:

1. ***Follow your system and keep emotion out.*** These types of tenants are basically just thieves. But they are also extremely frustrating, much more so than just someone who steals your A/C unit, because the whole thing just drags on and on. You just have to see this as a cost of business and move on, though. Getting angry will likely lead to a mistake, so just follow your procedures, be patient, and don't take it personally. Remember, professional tenants may get a free place to stay, but they don't get rich, which is what we're trying to do.

2. ***Follow the law carefully.*** It's best to use an attorney here and do everything by the book. These tenants will often take advantage of small mistakes to drag things out or get concessions. Indeed, I've heard of attorneys who just look over eviction fillings for minor mistakes so they can contact the tenant and sue the landlord. Be careful.

And Finally

The most important piece of advice, other than screening, is simply to see bad residents as a cost of doing business. Don't let one bad one turn you off from real estate or even just ruin your day. It's just a cost. Think of it like a furnace going out. Just fix it and move on.

CHAPTER 9
REFINANCING DEBT FOR LONG-TERM HOLDS

BRRRR: **B**uy—**R**ehab—**R**ent—**R**efinance—**R**epeat

> ➢ **BACK TO HOME PLATE —Bank Refinancing and Accounting**

A while back we were talking with a partner who was bemoaning the debt we were taking on even though we had an increasing amount of cash flow to cover that debt. It gave me the opportunity to share a secret of mine. Other than when talking to banks, I never value our company on the basis of its equity. I value it on the amount of debt it has. Why? Because real estate business builders are always focused on leverage. There are four questions to ask ourselves:

1) What new value-add purchases, leveraged with debt, can we make that will increase our positive cash flow?
2) How can we further leverage our current property portfolio more effectively to safely stretch our available cash?
3) What do we need to hold in reserves (i. e. not leverage) in order to keep on hand adequate liquidity for rainy days and opportunities?
4) What can we do to reduce our cost of funds on our overall debt?

Simply put, we love debt. Likewise, we hate debt; bad debt. Rent-to-own televisions, computers, and furniture—and even things like car loans—are simply transfers of wealth from the impatient to the patient. Bad debt simply means you are obligating yourself to work in the future to pay off whatever you're buying today. You're demanding your future self to work to pay off whatever pleasure you are enjoying in the here and now."

Let's Talk about "Bad Debt"

Bad debt habits often start with credit cards. We love credit cards because they simplify our lives. They also tempt us to make purchases that we would not otherwise make. Worse yet, if we do not pay off our credit cards every month, something 55% of Americans don't do we enter the financial trap of revolving debt.

The average interest rate we are paying on revolving credit card debt is above 16.5% interest which means that for those carrying such debt they are paying nearly $1,000 per month. There is no good way to start a wealth building strategy when you have one hand tied behind your back financially with such bad debt.

But bad debt doesn't stop with credit cards. Here are other sources of debt, which excluding mortgage debt (we'll talk more about this) is potentially bad debt. Here's 2019 states NerdWallet:

Type of debt	Total owed by an average U.S. household with this debt	Total owed in the U.S.
Any type of debt*	$135,065	$13.67 trillion
Credit cards (revolving)**	$6,741	$423.8 billion
Mortgages	$185,591	$9.24 trillion
Auto loans	$27,630	$1.28 trillion
Student loans	$47,634	$1.49 trillion

** This debt can include mortgages, home equity lines of credit, auto loans, credit cards, student loans and other household debt, according to the Federal Reserve Bank of New York.*

***The credit card debt figures in this chart represent revolving credit card balances — those that are carried from month to month — rather than all credit card balances. Total U.S. credit card outstanding debt stands at $949 billion, which includes both revolving and transacting balances.*

Bad debt is debt put on depreciating items like almost anything we purchase new. Take buying a new car as an example. The second we drive a new car off the lot it loses 20% of its value and, unless we put 20% down, we are immediately in negative equity territory. If we've financed that car, we've created bad debt. If we paid cash, we haven't done better because we have lost an opportunity for whatever else we could have done with that cash.

There are sound justifications to buy new, but most of the buy and hold investors I've known are masters of delayed gratification, so much so that they often become "permanently disabled" when it comes to taking on bad debt or using cash for unwise purchases. What was once a matter of necessity and opportunity becomes so ingrained it becomes a matter of lifestyle.

Let's Talk about "Good Debt"

Good debt is financing that is used to increase cash flow above the debt incurred. Creating and increasing positive cash flow is *THE GOAL* which enables you to build a formidable buy/hold business with an expanding array of opportunities for yourself and your team.

Is Delayed Gratification Really Worth it?

So, just in case you had some final reservations, here's the gold standard proof that delayed gratification is a good thing and worthy of your pursuit (and something to instill in your kids). It comes from a 1972 study known as the Stanford Marshmallow Experiment.

In the '60's Stanford professor Walter Mischel conducted an experiment on hundreds of five-year-old children which revealed the likelihood of success in their later work, life and health.

The experiment went like this. Each child was brought into a room with a marshmallow placed in front of him or her and the following instructions: You can eat the marshmallow any time you want or, if you wait for the researcher to come back, you will be given a second marshmallow. So, one treat now or a double treat later which ended up being a waiting period of about 15 minutes.

Apparently, there is video footage of the antics some of the children went into to—jumping, wiggling, bouncing, scooting around—to try and avoid eating that marshmallow About two-thirds however, succumbed to the tempting treat but a minority managed to wait it out.

Now here’s where it gets interesting. In subsequent years the children and their progress were tracked and a very discernible trend showed up. Those willing to delay gratification, waiting to receive the second marshmallow, ended up scoring higher on their SAT’s, had lower amounts of substance abuse, lower rates of obesity, lower stress, a higher degree of social skills, etc. as reported by their parents.

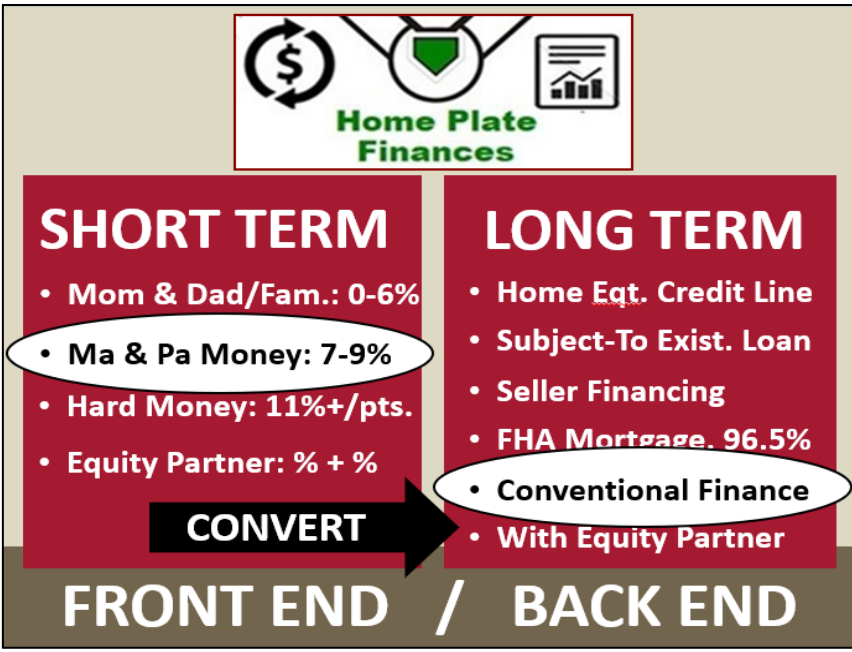
Which group do you want to be a part of? Are you willing to wait for that second marshmallow…the future wealth that comes from exercising present discipline or will you settle for treating yourself now?

Even if you don’t feel you’re good at delayed gratification you can start making better choices and building better habits. Make a plan, find an accountability partner and start today. That 2nd treat is well worth it!

The BRRRR-Gap Challenge

The backend of the BRRRR strategy (when we round the bases to get back to Home Plate) comes from the longest term, lowest interest financing available and that’s with banks. Once an investor has ten loans, they are no longer qualified for Fannie Mae/ Freddie Mac backed loans, which provide the best terms available for residential lending. So, we look to banks that “portfolio” their loans, keeping them in-house. These are usually from local or regional institutions that make *commercial loans on residential properties*, a niche loan product not offered by every bank.

Our BRRRR-Goal is to refinance out all our cash on each deal within one to two years from acquisition and to remain cash flow positive in the process. "BRRRR-ing Out" is the number one reason to get great deals in the first place, but such a goal can be quite challenging, especially in more expensive costal markets. Since this is our aim—*fully financed, positive cash-flowing, with none of our own cash in the deal*—this goal informs which markets and submarkets we target.



Many banks require a 12-month seasoning period before they lend on a property's appraised value. Thus we want to borrow private money for at least 18-months to provide a cushion. We focus on banks who loan at 75% of the *appraised value* of the property, not on the basis of our total cost into the property (which is hopefully lower!), thus giving us the highest possible loan-to-value refinance.

Again, our goals are to 1) get all, or nearly all, of the capital back that we've used to buy and rehab the property, 2) to lower our cost of funds (currently 5.5% interest or so) and 3) to stay cash flow positive.

Therefore, we want to keep our all-in costs as close to 75% of the property's post-rehab value as possible. Otherwise, we end up "subsidizing" the deals with our own cash which runs out sooner or later.

Given that our company has strong equity and we buy in volume, we are okay with the all-in cost going over 75% of a property's appraisal from time to time, and thus, leaving some of our capital in the deals (though it's not ideal). Over time, however, we want to get out all of our funds, and the way we do that is through the BRRRR-RRR strategy.

The BRRRR-<u>RRR</u> Strategy

I (Bill) once calculated that I've paid off less than .025% of the properties that I have owned. Instead, I am, and we are, busy with an extended version of BRRRR. While the last "R" in the formula refers to repetition with a *new* property, one could change it to mean with the *same* property:

BRRRR-RRR: Buy—**R**ehab—**R**ent—**R**efinance—**R-R-Repeat…**

Relax (wait)—**R**efinance (again) and—**R**epeat (on the same property)

The waiting period may take five, 10 or even 15 years depending on the amount of equity paydown, appreciation, additional upgrades, and rent increases that justify the cost of refinancing. But it's surprising how quickly those refinancing opportunities come back around.

We've added as many as three additional sets of R's to the BRRRR strategy on some pieces of property (BRRRR-RRR-RRR-RRR), thus freeing up a huge amount of additional capital over time. Each time we leverage through borrowing, we increase our Return on Investment (ROI), because we are reducing whatever down payment and rehab funds we personally have in the property.

After the second, and certainly by the third refinance, we have received back our down payment and upgrade funds thus making our ROI an infinite one. Although refinancing puts debt back on the property, and with it, likely higher monthly mortgage payments, it also creates tax-free capital with which we can reinvest.

Properties serve as people's homes, where their kids grown up, their pets roam and memories are made. But for us, they are a commodity on which we leverage debt (with lender's money) and service debt (with resident's rent). Over time those properties can be used as "refinancing debt instruments" to expand our portfolio and operation.

Getting the Long-Term Loans You Want: Eight Refinancing Steps

Here is a step-by-step guide to getting your BRRRR property across the finish line to flip your front-end, short-term financing to back-end, long-term financing.

Step 1: Look for a Lender (And Cast a Wide Net)
One mistake a lot of people make is to only start looking for a lender once they need one. Start looking for, vetting, and building rapport with lenders early on in the process. This saves you a lot of time when you actually want to get one. And if you have a private or hard money loan on the property while you are doing the repairs, the holding expenses will add up as you scurry around looking for a bank.

Furthermore, in the process of looking for a lender and submitting financials, it may highlight problems you have with your credit or income that you need to resolve before pressing forward.

The best way to find a good bank is to ask other real estate investors who they are using. Banks can always add new clients without short-serving their current ones, so people will be happy to give referrals. Indeed, no one has ever turned me down for this request.

And always make sure to let them know who recommended you. That acts as a sort of social proof: "Hey, if we lent to this other person, and that person knows you, then you're probably also a good person to lend to." And again, for more ways to find banks, see here.

Of course you can also just call random banks and say something like, "I am a real estate investor looking to refinance single-family investment properties. Is this something your bank would be interested in?" Usually, you'll get a quick "No" if it's not something for which their looking.

Step 2: Drill Down to Make Sure The Bank Works for You

Some banks just aren't interested in lending on investment properties. Some want long seasoning periods (the time you need to own a property before they will lend *on appraised value* and not just the amount of cash you have into the property), and others have so-so terms and rates. You have to sift through a lot of coal to find a few diamonds.

Personally, I (Andrew) like to try to add a new bank to our catalog every so often even if we have a bank willing to do business with us. This is not just because I might find better rates. It's also because sometimes banks will lose their appetite in what we have to offer. I want to be able to quickly go to another bank that we have already built a relationship with.

Step 3: Build Rapport with the Lender

People like doing business with people they like. This cannot be overstated enough. Lenders are not cybernetic automaton. They are flesh and blood human beings. There seems to be this myth floating around these days that lending has become so dominated by mathematics, regressions, and algorithms that you will either be accepted or not based on the numbers that show up on your tax return and credit score. This is simply not true.

When your lender vets your loan with the bank's underwriter and gets a tentative okay he or she then takes your loan to the bank's loan committee. Your lender is there to sell the property and more importantly, to sell you. If that lender believes in you, more often than not, you will get the loan you are looking for. If he or she does not, then you probably won't. It's not hard to tell when someone is unenthused, and the loan committee will be able to pick up on this quite easily.

If they sense hesitation in the lender presenting your loan, you will likely be rejected. Your goal has to be to sell the lender so the lender will sell the committee. And of course, first and foremost, you've got to sell the lender to even take a look at your loan!

Therefore, it's a good idea to take the lender out to lunch or bring him or her to your office if you have one. Describe your life story, your business, and your strategy and let your passion for the business shine. Make sure they know you care about this and are deeply invested, both financially and emotionally. Make sure you also know what you are talking about. Review your personal finances and the information regarding whatever property you are trying to refinance.

You want to come off as an expert, as banks obviously want to lend to people who know what they're doing. Finally, ask the lender what the bank is looking for to make sure you aren't wasting their time. They will appreciate this, as most people these days only care (or act like they care) about themselves. And, of course, never be afraid to engage in a little rapport-building chit-chat. And make sure to buy lunch! There's something called the Rule of Reciprocity that can work in your favor here.

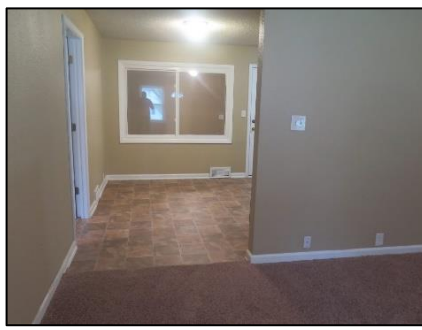
Step 4: Get Your Financials In Order (a Confused Mind Says No)
I can't even begin to count the number of times I've been looking at properties to buy where the owner's financials are such a mess I can't make heads or tails of them. This is the good ole "Ma and Pa" accounting that you need to avoid like the plague.

Make sure to use a reputable accounting program such as Quickbooks or a property management software with a good accounting module like RentManager. And if you aren't good with accounting, then you need to find someone to take care of it.

Regardless, don't think of bookkeeping as "just something that needs to get done — or whatever." It is vitally important to keep good, easy-to-read books. If a lender looks at your financials and can't make sense of them, she'll usually just say no. Why bother trying to figure it out if she can move onto a potential loan that's easy to underwrite?

Furthermore, your financials project how organized and professional you are. If your financials are a mess, then the lender will probably think you and your business are as well.

Step 5: Make Your Property Shine (First Impressions as They Say)
Banks don't want to lend to slumlords any more than renters want to rent from them. One of the best ways to get a bank to believe you know what your doing is to present them with a very nice-looking, functional and clean property. Yes, you don't want to rehab out the equity of a property (a common mistake BRRRR investors make), but you need to make it look nice. For example, the following are pictures of a property we recently refinanced:



As you can see, nothing in this property is particularly fancy—regular carpet and vinyl flooring, basic appliances, standard Home Depot cabinets, Formica countertops, etc. In nicer properties, you may very well want to go with higher end materials. But that's beside the point. The important point here is that the house is very clean, everything looks good, and everything is functional. Trust me, this is not what many banks normally get. Bringing something like this to them proves your professionalism and expertise more than any mere words can.

Of course, you'll want to have the property rented before you send it to a bank to get refinanced, but you should send them all of your marketing pictures. Which leads us to the next part.

Step 6: Document Submission (Another Chance at a First Impression)
My goal when submitting documents to a bank is not to give them everything they need, it's to blow their socks off. I go over my strategy in more detail here, but the short version is I send them a Dropbox folder (or flash drive) with a list of all the partners' financials, the company financials, business plan and documents, as well as all of the property financials, a pro forma, and lots and lots of pictures.

This will make you look all the more competent as well as provide the lender with all the documents they need (and more). Remember, it's critical to impress the lender so that he or she will sell you to the loan committee. It's also important to give them everything they need to make an decision, because a confused mind almost always says "no."

When you submit your documents, make sure to submit everything you can and in a clear and easy-to-follow way. I try to impress the lender here, too, in order to prove my professionalism and competency. Again, this lender is going to be your advocate. You should try to impress her. I usually submit personal financials, tax returns, property financials, a rent roll, pictures of the property, my resume and business plan, and anything else that makes sense to send. I do this by putting it in a Dropbox folder with several sub folders.

Step 7: Keep your cash flow high.
Banks love cash flow. They want the property to have at least a 1.2 DSCR (debt service coverage ratio: debt service divided by net operating income), and they also want you to have a strong "global cash flow." So, it's keep your cash flow as high as possible. Any work on a property that can be justifiably capitalized (put on the balance sheet instead of the operating statement) should be.

And while we all like to talk about quitting our job to go into real estate full time, you need to be cognizant of what this may do to you in the eyes of banks. Bank really, really love W-2 income. I'm not saying you shouldn't quit your job and go into real estate full time, but you may want to talk to some banks about it first, especially one's you've built a relationship with. You might also want to get your refinances completed before you consider making the switch.

But overall, the numbers, while very important, aren't the be-all, end-all of getting a refinance. Banking is still a people business and you need to master the art of coming off professional, competent and enthusiastic for the business. If you follow all of these steps, you should be able to get your refinance loans approved more often than not.

Which leads us to…Step 8: Make sure to attend the appraisal.
Appraisers are people to and affected by who they meet at the property they are appraising along with the property itself. If they are impressed with you: your confidence, knowledge and information regarding the comps (for this property) along with what rehab you've done, the more that will be seen in a strong appraisal. So, make sure to attend the appraisal to ensure you property is presented in the best possible light.

The road to riches is paved with borrowed money.

Show me a millionaire, and I will show you, almost invariably, a heavy borrower…. Millionaires, like banks, are made of borrowed money.

Capital is the lifeblood of your progress. To insure success you should keep it continually working for your benefit.

Borrow the maximum that can safely be repaid. Buy only property that needs improvement. Make selective improvements that increase value.

-Bill Nickerson, The Godfather of Modern Buy & Hold Investing
How I Turned $1,000 into a Million in Real Estate--in My Spare Time
Editions: 1959—One Million / 1969—Three Million / 1980—Five Million

YOUR COMPANY
The BUSINESS of Wealth Creation

I am a better investor because I am a businessman, and a better businessman because I am an investor. -Warren Buffett

All progress takes place out of your comfort zone.
-Michael Bobak

I find that the harder I work, the more luck I seem to have.
-Thomas Jefferson

Success is walking from failure to failure with no loss of enthusiasm. -Winston Churchill

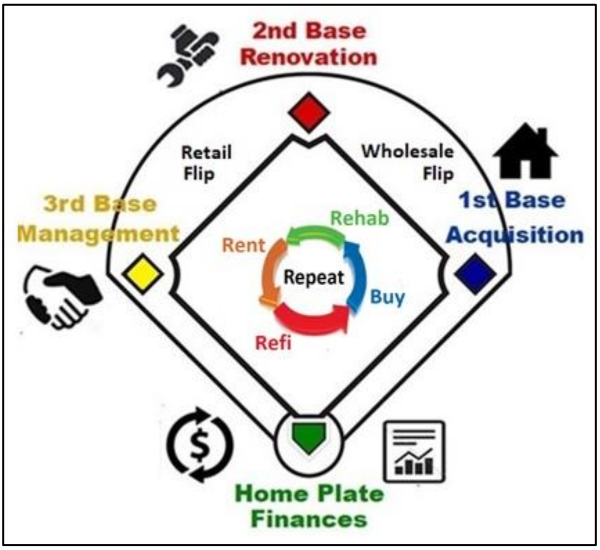
Try not to become a person of success. Rather become a person of value. -Albert Einstein

CHAPTER 10
SCALING YOUR RE BUSINESS INTO A COMPANY

For a company to progress from Good To Great, to use Jim Collins' phrase from his book by the same name, requires many, many consistent turns of its "flywheel." At some point after all those turns, momentum takes over. This doesn't mean that we can now ease up. It just means that the same consistent pressure can continue to be applied to the flywheel and it will keep spinning out quality results.

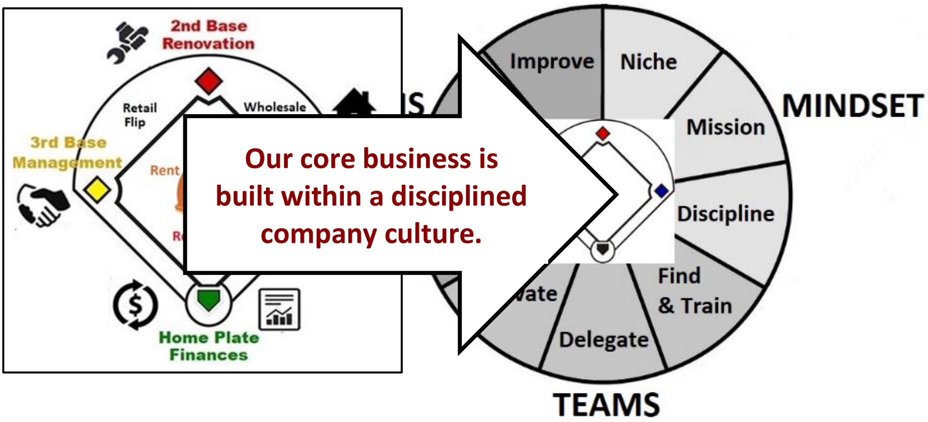
Our flywheel, described by the baseball diamond analogy, has buy and hold investors looking to hit good pitches from motivated sellers with discounted properties and then running the basses, time and again.

If our team continues to deliver a solid performance, momentum will carry us forward so that even a periodic strike out, ground and fly out, will not alter the outcome of the game. On the other hand, occasional home runs are certainly appreciated but it is consistent hits and base running that leads to ongoing success on the field.



However, baseball is much more than what fans see on the field. There is an enterprise that supports the team: owners, managers, scouts, fans, and facilities to name a few; all of which make up the business of baseball.

And so it is with real estate. There's real estate investment—buying and selling and/or holding a few properties, and then there is developing the necessary mindset, teams and systems to scale the business from a small operation into a substantial company.



Addressing Your First Obstacle to Growth: FEAR

Did you feel nervous about buying your first home or investment property?

Have there been times you've suffered from "buyer's remorse" after sitting back and reflecting on a particular property purchase? How about when you hired your first employee and started a pay-roll—was that a little scary?

Stepping into the unknown necessitates taking risks and it is those risks that can paralyze us in fear of making a wrong decision.

Fear is not necessarily bad. It's an emotion meant to get our attention. Have we done all the due diligence that we should before making this purchase or expanding in a certain way?

But what we should fear more than making a mistake or doing something stupid is regret, the fear of missing an opportunity. If we had to choose between the two, we'd rather live with the title of "loser" than the agony of shoulda, woulda, coulda.

What do you fear most when it comes to growth?

Whatever it is, maybe you too should fear regret more. If you sit on the sidelines, worried and waiting what are your opportunity costs? Which deals are you missing, and could they have helped you build a financial foundation of success that is still waiting to happen? Don't look back five years, or ten or twenty from now contemplating what might have been. If you must fear something, fear lost opportunity.

Fear of lost opportunity emboldened me (Bill) to drop a comfortable but counterproductive informal business style. For example, I stopped meeting tenants at my home to do rental agreements and established an office: a table at Wendy's restaurant. My next office amounted to two rooms carved out of a rental house close to a commercial district.

I still remember walking into that office after hiring employee #2. I looked around and said to myself, "Bill, you've actually got a business going on here. Wow, didn't see that coming!" But every time I took on fear of the unknown and forced myself out of my comfort zone, new and exciting opportunities presented themselves.

Another milestone came later when a workout buddy brought his son to the gym. He introduced me to his son as his "millionaire friend." The statement was, frankly, jarring. By that time, I was actually his "multi-millionaire friend," but I had never thought of myself in such stark financial terms, and to hear someone say it out loud gave me a moment of consternation and pause. I wasn't embarrassed, but rather silently gripped by yet another fear: "To whom much is given, much will be required."

We're not suggesting everyone needs to grow in a certain way or to a certain point. We're all unique with our own inclinations, set of circumstances and distinctive goals. What we would say is that we will never break through to meaningful milestones without facing down fear. Listen to the consequences of fear in our lives articulately described in *The Rose*.

It's the heart, afraid of breaking, that never learns to dance.
It's the dream, afraid of waking, that never takes the chance.
It's the one who won't be taken, who cannot seem to give.
And the soul, afraid of dying, that never learns to live.

-*The Rose* by Amanda McBroom (popularized by Bette Milder)

Risk-taking courage, in all its forms—personal, spiritual, relational, business—is so essential to our personhood, that, without it, something inside us dies. “Those who aren’t busy being born,” to quote Bob Dylan, “are busy dying.” If we settle for idling in neutral, our life experience does little to encourage, inspire or motivate even ourselves. Treading water, to change the analogy, might keep us from drowning but it won’t get us anywhere.

“Those who aren’t busy working to improve their business life,” to apply Dylan’s quote to the topic at hand, “will eventually witness that business deteriorate and decline.” But “busy working” does not necessarily mean increasing our workload or working longer hours.

I (Bill) remember a trip driving back to my folks’ house in Wichita, Kansas from the Colorado Rockies many years ago. Somehow, I turned south at one point instead of east and drove for hours right toward New Mexico before I finally figured out my error and took an eastward turn. All that time I was busy driving hard. I just wasn’t driving smart.

So, what does it mean to drive smart? It all begins with the driver. You are both your company’s principal asset and its primary obstacle. Maybe this won’t always be true. You may very well entrust someone(s) more capable than you to run your business, maybe you already have: a key employee or a partner.

When you do find and train the right people and see them excel (more about this in Part 3), it’s quite a joy watching them exercise skills you will never possess and taking your company to heights you never anticipated. A-players accelerate your business exponentially while C-players drag you backward, costing you an immense amount of time, energy and money.

But don’t blame them. You hired them. You’re the leader and leaders take hiring very seriously. It’s one of the most important things you do to empower or enfeeble your organization. If you want to grow and build your organization from mediocre to good to great hiring and partnering with the right people is your KEY objective.

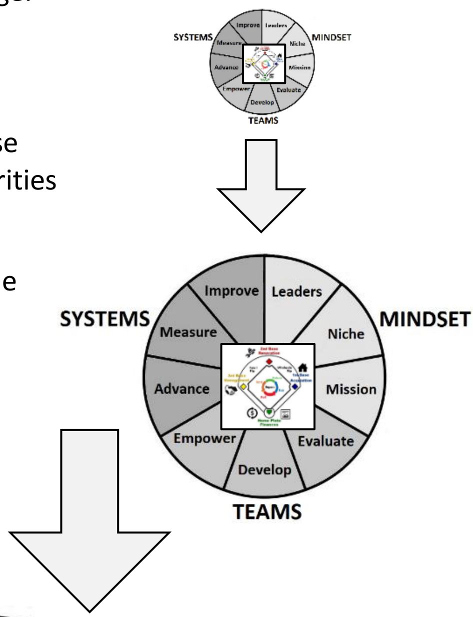
There are numerous real estate investment books and online resources suited to growing a real estate business from A to B. Likewise there are several resources on to how to grow a business once started. But there precious few resources specifically tailored to growing a real estate investment business past point B, where most investors find themselves, to C, D, E and beyond, where many would like to go.

Most businesspeople don’t think large enough to create something large. 90% of US companies would be of the “mom & pop” variety, with four or fewer employees. To grow large, we’ll need to “surround our baseball diamond” with the mindset, teams and systems to scale. Are you ready to build your real estate business? If so, the second half of this book will help by zero in on nine growth-producing steps.

While these nine essential qualities are present in every size successful business, they require new and adjusted skill sets and priorities as a company grows from a small operation to a larger enterprise. This new skill set gets practical application from questions that we include at the end of each chapter.

Depending on our skill level or that of our organization, there is a point at which most of us as business owners get stymied: How do you break through the natural barriers to growth at each level? What does it take to grow teams of highly effective people who consistently work highly efficient systems? Herein lies the need to look for a coach who has “been there, done that,” to take you to the next level. While we can’t help you with all the specifics you will need, we’ll give you a good start.

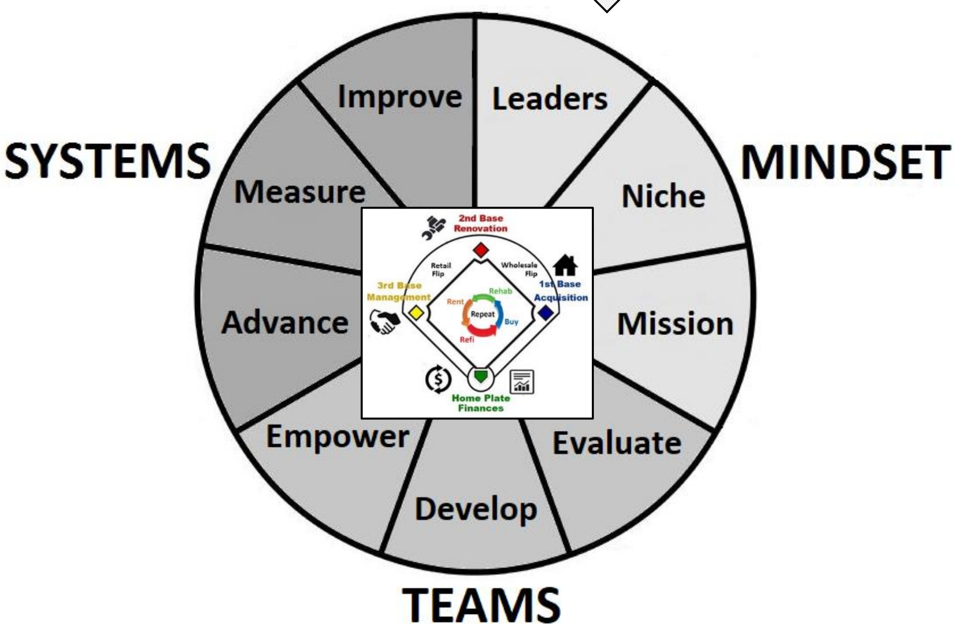
So, with some fear and trembling ourselves, we step into this under-served gap and describe how to scale your real estate investment business from small to medium to large.



—Big-Thinking MINDSET
1) **LEADERS** embody the vision
2) **NICHE-THINKING** breeds expertise
3) **MISSION-MINDEDNESS** sets priorities

—Highly Productive TEAMS
4) **EVALUATE** to find the right people
5) **DEVELOP** a results orientation
6) **EMPOWER** others to excel

—Execution of SYSTEMS
7) **ADVANCE** strategically
8) **MEASURE** consistently
9) **IMPROVE** continually



PART 2
BIG-THINKING MINDSET

Start from wherever you are and with whatever you've got. Don't say, 'If I could, I would.' Say, 'If I can, I will.

You cannot change your decision overnight, but you can change your direction overnight.

Your personal philosophy is the greatest determining factor in how your life works out. How long should you try? Until.

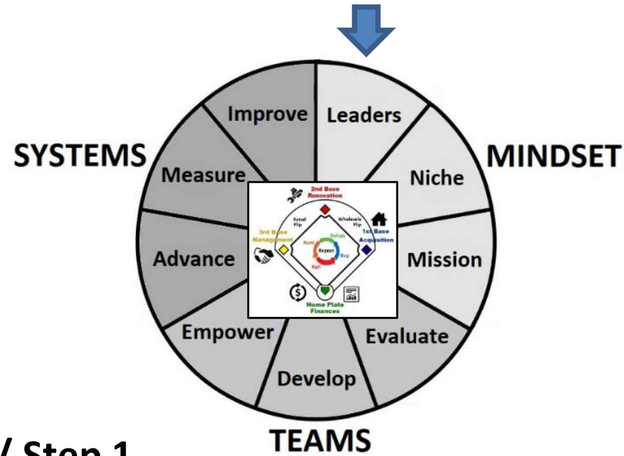
Success is neither magical nor mysterious. Success is the natural consequence of consistently applying basic fundamentals.

If you go to work on your goals, your goals will go to work on you. If you go to work on your plan, your plan will go to work on you. Whatever good things we build end up building us.

Set a goal to become a millionaire. Why?
Answer: For what it will make of you to achieve it. Once you've become a millionaire, you can give it all away because what's important is not the money but the person you've become. Set the kind of goals that will make something of you to achieve them.

-Jim Rolm quotes, the last one from his mentor, J. Earl Shoaff

https://www.brainyquote.com/authors/jim_rohn
https://everydaypower.com/jim-rohn-quotes-2/



CHAPTER 11 / Step 1
MINDSET:
Leaders embody the vision

Good business leaders create a vision, articulate the vision, passionately own the vision, and relentlessly drive it to completion.

-Jack Welch

If you are the leader, you embody the vision. Who you are, what you do, how you do it and why you do it sets the sails of your vessel and, as others join you, your flotilla. Your vision comes first from "me" and then "we," first singular but then, as quickly as possible, plural.

However large your company, don't expect the vision for it to come from anyone other than you and the original partners/principles, at least not at first. Once you've established a team of people who share the vision, then a dramatic, visionary multiplication process can take place which helps eliminate directions inconsistent with the vision and puts energy behind those that enhance the vision.

But, whether it's just you or it's you and your team, vision starts, continues and ends with the quality of leadership provided. And that's how it should be. The only question is: What kind of leadership will you provide? and, by extension, will your team provide?

In his classic book, *Good To Great*, Jim Collins describes how he initially encouraged his research team to NOT consider leadership as a significant factor as they studied the dynamics what makes good companies great. Leadership, he contended, just seemed too overstated. But, after the data came in, he could no longer resist the evidence. Leadership, he contends, is not *a* factor of success; it is *the* factor of success.

For the book Collin's Stanford research team spent 25,000 hours, starting with 1435 companies and selecting just 11 which were mediocre for at least 15 years and then became great with a performance 7 times greater than the average for a period of at least 15 years. They found these company's leaders possessed a contradictory combination of characteristics: 1) a deep humility, and 2) an intense will.

Such leaders powerfully lead, but they do so without the need for personal focus or credit. They are highly driven individuals but not so much for their own success as for the success of their vision and cause, and the people and organization that represents and implements it.

They take blame when there are setbacks and direct praise to others when there are successes. When asked about their own contribution they often talk about how lucky they were to be at the right place at the right time with the right people. But luck has little to do with it!

Collins says he considered calling this dynamic mix of humility and determination *servant-leadership* to contrast it with other, lesser forms of leadership. Instead he coined the term "Level 5 Leadership:"

To quote Collins: *Level 5 leaders display a powerful mixture of personal humility and indomitable will. They're incredibly ambitious, but their ambition is first and foremost for the cause, for the organization and its purpose, not themselves. While Level 5 leaders can come in many personality packages, they are often self-effacing, quiet, reserved, and even shy.* ***Every good-to-great transition in our research began with a Level 5 leader who motivated the enterprise more with inspired standards than inspiring personality.***

PERSONAL HUMILITY	PROFESSIONAL WILL
Demonstrates a compelling modesty, shunning public adulation; never boastful.	Creates superb results, a clear catalyst in the transition from good to great.
Acts with quiet, calm determination; relies principally on inspired standards, not inspiring charisma, to motivate.	Demonstrates an unwavering resolve to do whatever must be done to produce the best long-term results, no matter how difficult.
Channels ambition into the company, not the self; sets up successors for even more greatness in the next generation.	Sets the standard of building an enduring great company; will settle for nothing less.
Looks in the mirror, not out the window, to apportion responsibility for poor results, never blaming other people, external factors, or bad luck.	Looks out the window, not in the mirror, to apportion credit for the success of the company – to other people, external factors, and good luck.

The Yin and Yang of Level 5

Some of Jim Collins' resources:

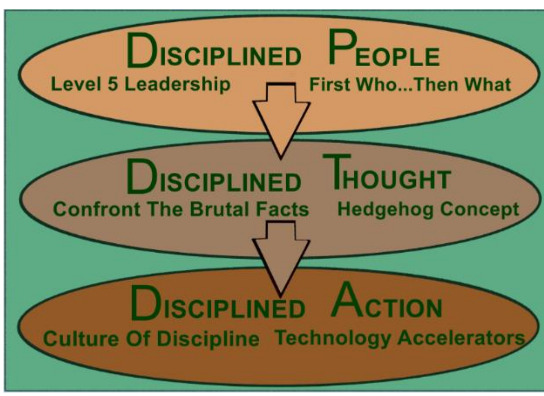
Built To Last:
amazon.com/Built-To-Last

Good To Great:
amazon.com/Good-To-Great

Great By Choice:
amazon.com/Great-By-Choice

Website Resources:
JimCollins.com

The key takeaway from *Good To Great* is *discipline*. To go from a good organization to a great one a company needs a level 5 leader who finds and develops disciplined people who embody disciplined thought and disciplined action.



- **Disciplined people** ensure that the right people are placed in the right jobs, that the wrong people are moved out quickly and that the best people focus on the biggest opportuneities.
- **Disciplined thought** means being honest about the obstacles you face and focusing on your "hedgehog concept:" 1) what you're most passionate about, 2) what you can be the best in the world at and 3) what drives your economic engine.

- **Disciplined action** develops a culture of discipline that employs every means available, including technological ones, to meet the objectives of the organization.

When you think about a business, the lowest level of leadership comes from individuals who are highly capable. They use their know-how and hard work to contribute to the company's efforts.

The next level are those who work well in a team, helping to make the whole of the team's work greater than the sum of its parts.

The third level includes competent managers who organize their teams to efficiently accomplish the goals they set.

Level 4 is where most good leaders end up. They receive a commitment from their managers to pursue the company's mission and get their work done in an efficient and effective way.

Finally, at the pinnacle, we find Level 5 leaders—the rare GREAT ones. They have all the qualities of the other four levels plus a unique combination of self-effacing humility and iron, even fanatical determination to produce exceptional and sustainable results.

My [Jim Collin's] *hypothesis is that there are two categories of people: those who do not have the seed of Level 5 and those that do. [The first] could never in a million years bring themselves to subjugate their egoistic needs to the greater ambition of building something larger and more lasting than themselves. For these people, work will always be first and foremost about what they get--fame, fortune, adulation, power, whatever--not what they build, create, and contribute.*

….[The second are] those who have the potential to evolve to Level 5; the capability resides within them, perhaps buried or ignored, but there nonetheless. And under the right circumstances--self-reflection, conscious personal development, a mentor, a great teacher, loving parents, a significant life experience, a Level 5 boss, or any number of factors--they begin to develop.

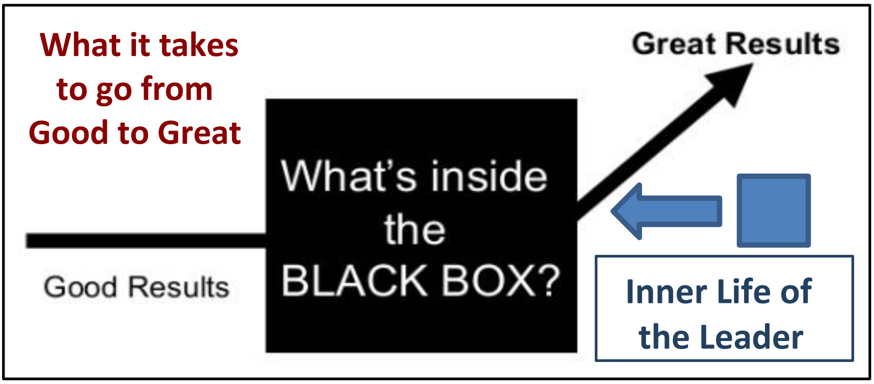
...Our research exposed Level 5 as a key component inside the black box of what it takes to shift a company from good to great. ***Yet inside that black box is yet another black box--namely, the inner development of a person to Level 5 [emphasis mine].***

Here's the question that Jim Collins answers and we elaborate on especially for real estate investors:

--What is in the black box that turns a company from good to great?

But here is the question that remains UN-answered in Collin's book:

--What is in the inner box (the life-development of the leader) within the black box of what turns a good company into a great one?



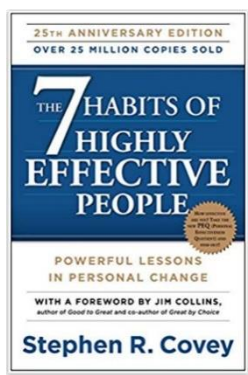
We will now seek to answer Collin's unanswered question...regarding how one can cultivate their inner life to become a level-5 leader.

Good to Great Starts with the Inner Life of the Leader

Never expect your enterprise or organization to be better than you. That doesn't mean you bring all the abilities and resources to its efforts—not by a long shot. But what it does mean is that success starts by how you cultivate your inner life to form your private thinking and make your decisions. It all starts with "the inside" that those around can't see but will, no doubt, experience "the outside" results.

For our purposes we're talking about leadership within a real estate investment business. But the question can certainly be expanded. You're not likely THE leader in every context, but you likely provide some form of leadership wherever you go. So, what kind of leadership do you bring to groups with which you are associated—your family, a work team, your church or social organization, or a company?

You might want to look at the pyramid again on page 174 and evaluate where you are in your leadership abilities on a scale of 1 to 5: ______ Where do you want your leadership to be? ______ This is deceptively simple but extraordinarily challenging question. If you aspire to Level 5 Leadership, I'd encourage you to read Stephen Covey's book, *The 7 Habits of Highly Effective People.*



Becoming a Level 5 Leader

Okay, I (Bill) am now writing beyond my own personal ability and experience. But this I know: To become a Level 5 leader you first must want it and want it bad. I point you to Stephen Covey's perspective. He answers the question of how a person aspires to Level 5 and we will focus on **Covey's first three habits** in what follows.

Level 5 leadership, in any realm, is very rare. If you are up for aspiring to such rarify heights yourself, what follows is the only way I know how to work at getting there.

The Inner Life of the (Good to Great) Leader

Dream as if you'll live forever. Live as if you'll die today.

-James Dean

Your life is but a wisp of fog, catching a brief bit of sun before disappearing. -The Apostle James, 4:15

START HERE FIRST: Knowing the reality of death should rearrange our priorities. It reminds us of what's important. Instead of putting things off, facing death helps us get busy living and avoid misplaced priorities. **Check below to identify some past misguided priorities. *I WISH I…***

_____ Had the courage to just be myself.
_____ Spent more time with the people I love.
_____ Had made spirituality more of a priority.
_____ Had not spent so much time working.
_____ Discovered my purpose sooner.
_____ Learned to express my feelings more.
_____ Spent less time worrying about things that never happened.
_____ Taken more risks. Pursued more of my dreams.
_____ Cared less about what other people thought.
_____ Realized earlier that happiness is a choice.
_____ Taken better care of myself.
_____ Been a better spouse/son/daughter/father/mother.
_____ Paid less attention to other people's expectations.
_____ Quit my job and found something I really enjoyed doing
_____ Had not spent time chasing the wrong things.
_____ Touched more lives. Loved more. Stayed in touch with friends.
_____ Thought about life's big questions earlier.
_____ Traveled more. Had children. Had more (less!) children.
_____ Lived more in the moment. Spoken my mind more.

I have only just a minute, Only sixty seconds in it. Forced upon me, can't refuse it, didn't seek it, didn't choose it, But it's up to me to use it. I must suffer if I lose it. Give an account if I abuse it. Just a tiny little minute, but eternity is in it. -Dr. Benjamin E. Mays

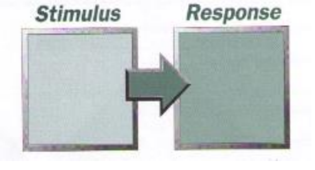
HABIT #1: Focus on being proactive rather than reactive.

Look back over the list you checked. You and I can't change the past, but we can change the future starting with today. Most people just let life come to them and then react from there. But Level 5 leaders are very different. They make an ongoing commitment to be change agents, first on themselves and then for those around them.

Granted, we all have different backgrounds, experiences and opportunities—some difficult, some exceptionally great, but everyone (even in desperately poor counties or in prison for their political or spiritual beliefs) can choose to live proactively, above their circumstances. The proactive choice of attitude is "the last of the human freedoms."

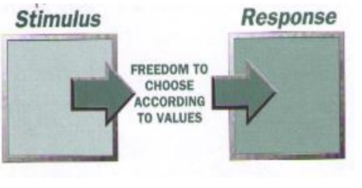
We who lived in concentration camps can remember the men who walked throughout the huts comforting others, giving away their last piece of bread. They may have been few in number, but they offer sufficient proof that everything can taken away from a man but one thing: the last of the human freedoms—to choose one's attitude in any given set of circumstances, to choose one's own way.

-Victor Frankel, *Man's Search for Meaning*



Reactive people allow outside influences (mood, feelings, circumstances) to control their responses. They are affected by the social weather around them.

Proactive people use the margin of freedom to make choices that best apply their values. Their freedom to choose expands as they wisely use the space between stimulus and response.



I'm not a product of my weather. I choose my weather wherever I go.

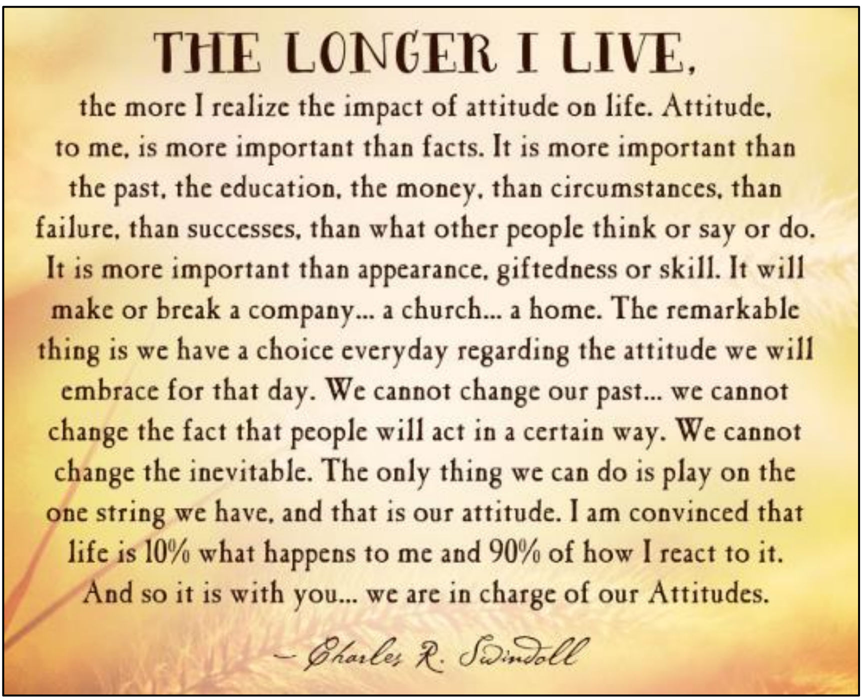
On a scale of 1 to 10 where are you with this being true for you? ___

How could you be more proactive in your life? __________________

____

____

What are your thoughts on this statement and how it applies to your life? (Write your thoughts below.)



____

____

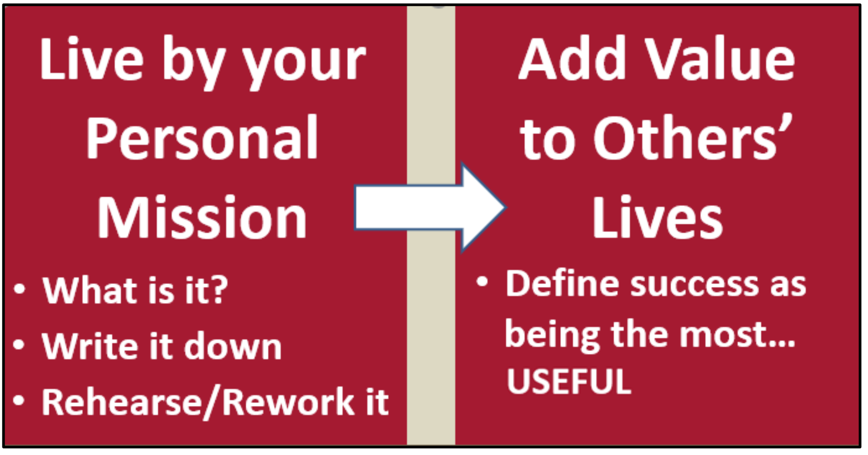
____

____

HABIT #2/Begin with the end in mind by creating a…

Personal Mission Statement to guide your life's decisions.

There are two primary issues in a leader's life. What will be my guiding principles in life and how will these principles affect the lives of others?



Mission Statement: A powerful document that expresses your personal sense of purpose and meaning in life: It acts a governing constitution by which you evaluate decisions and choose behaviors.

The Constitution of the United States is our country's mission statement. It defines who we are not by popular sentiment but by a set of principles. Our mission statement—for our self, our business or our family—likewise acts as our own constitution; what we stand for and hope to achieve through a life well-lived. It's our guiding values.

Personal Mission Statement Benefits (directly from Stephen Covey)
--Encourages you to think deeply about your life.
--Helps you examine your innermost thoughts and feelings.
--Clarifies what is really important to you.
--Expands your perspective.
--Imprints self-determined values and purposes firmly in your mind.
--Provides direction and commitment to values.
--Enables you to make daily progress toward long-term goals.
--Provides first mental creation of your desired results for your life.

Every physical creation (putting something into practice) starts with a mental creation—a thought, a plan, a perception or a motive.

FIRST CREATION (The Plan) >>>> SECOND CREATION (The Results)

A mission statement acts as a reminder of who you are and what you want to become. The storms of life will blow through your life but you have an anchor embedded in the rocks of previously set principles.

Look to mentors who exhibit Level 5 Leadership Qualities
I'm not sure I've ever known a Level 5 leader. Of course, I know high quality individuals who exhibited many Level 5 qualities, including my parents and my wife, but I've not known a Level 5 leader who embodied the whole package in a business context. What does it take?

The process of writing a mission statement involves answering a series of questions.
--What things do I want to have that I feel are important?
--What am I about?
--What are the qualities of character I would like to emulate?
--What legacy do I want to leave?

A Personal (–Family –Business) Mission Statement should:
--Be timeless. (goals are not timeless)
--Deal with all the important roles in our life.
--Not be a "dream" statement. It's not some pie in the sky ideal.
--Not be rushed. Feel free to edit and re-edit it often.
--Address the contributions and accomplishments that tie to your purposes and values. It answers the question, "What am I about?"
--Not to be put off. Why not start on it today?

Finally, envision your future memorial service. What tribute statements do you want the key people in your life to make about you?

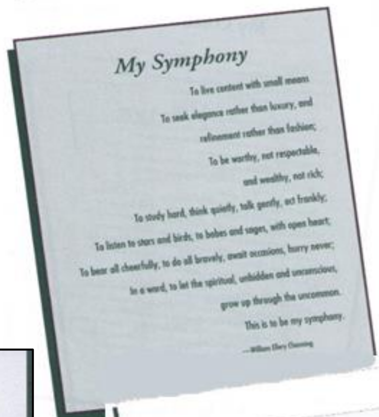
Family roles: –As father/mother –As son/daughter –As friend
Business roles: –As employer –As employee –As worker –As manager –As partner –As salesperson –As researcher –As director, etc.

Examples of Mission Statements

As you make decisions you want to evaluate them to see if they are in alignment with your personal mission statement to keep you on track. My (Bill's) personal mission statement is 70 words long but, at one point, I boiled it down to three key ideas to make it more memorable.

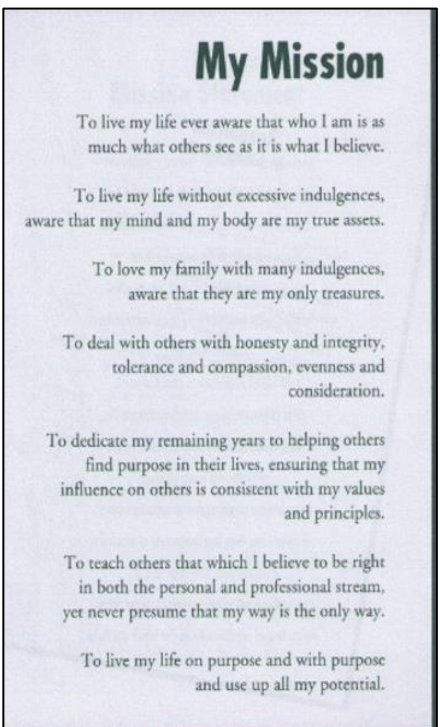
I am: –a *Recipient*
–a *Steward*
–an *Ambassador*

Will Smith has me beat when it comes to being concise. His mission statement: *I want the world to be better because I was here.* More examples:



My Symphony

To live content with small means
To seek elegance rather than luxury, and
refinement rather than fashion;
To be worthy, not respectable,
and wealthy, not rich;
To study hard, think quietly, talk gently, act frankly;
To listen to stars and birds, to babes and sages, with open heart;
To bear all cheerfully, to do all bravely, await occasions, hurry never;
In a word, to let the spiritual, unbidden and unconscious,
grow up through the uncommon.
This is to be my symphony.
—William Ellery Channing



My Mission

To live my life ever aware that who I am is as much what others see as it is what I believe.

To live my life without excessive indulgences, aware that my mind and my body are my true assets.

To love my family with many indulgences, aware that they are my only treasures.

To deal with others with honesty and integrity, tolerance and compassion, evenness and consideration.

To dedicate my remaining years to helping others find purpose in their lives, ensuring that my influence on others is consistent with my values and principles.

To teach others that which I believe to be right in both the personal and professional stream, yet never presume that my way is the only way.

To live my life on purpose and with purpose and use up all my potential.

Our Mission

The mission of our family is to create a nurturing place of order, love, happiness, and relaxation, and to provide opportunities for each person to become responsibly independent and effectively interdependent, in order to achieve worthwhile purposes.

The greatest value in life is not what you get but what you become. The major question to ask on the job, any job, in any relationship, is not what I am getting here. The major question to ask is what am I becoming here?

-Jim Rohn

Use the next two pages to start creating your mission statement:

Your Personal Mission Statement (roles to include)

SUCCESS:

NOT

Most Well-Off
Most Well-Known
Most Well-Liked

But the…MOST USEFUL

Your Personal Mission Statement (key issues to include)

OUR MISSION:

To be the most

USEFUL Person…

USEFUL Company…

the world has ever seen!

Your Personal Mission Statement (First Draft)

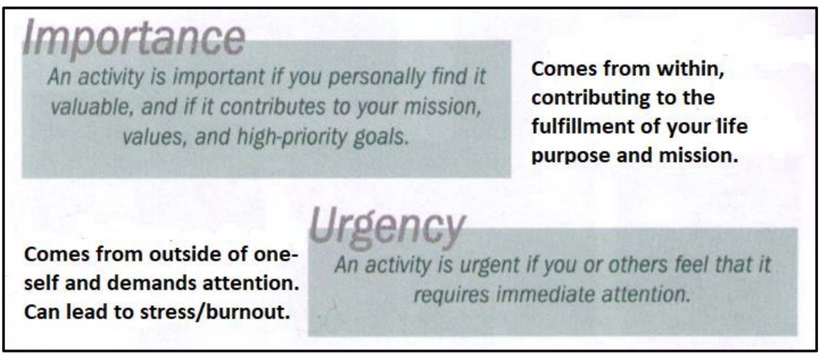
Your Personal Mission Statement (Second Draft)

HABIT #3/Put First Things First by…

Implementing your life mission into your daily schedule.

If Habit 2 says you're the programmer of your life, then Habit 3 says to write the program. This is the second creation of taking the steps and actions required to make the vision for your life a reality by examining our daily habits and routines. The critical question: *What are the most important things for you to do in this moment?*

Get into the habit of putting first things first by managing, avoiding and limiting the less important issues in your life and by focusing on what is important and aligned with your life's mission.



To do so, categorize things by their urgency and importance. Stephen Covey created a "quad chart" for this purpose as follows:

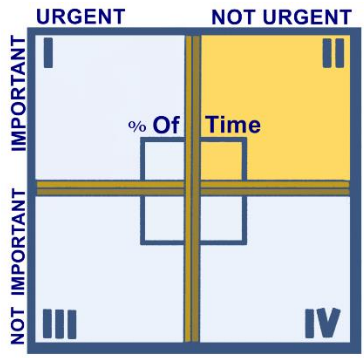
Quadrant 1—Urgent and Important (necessary but not value adding): A reactive mindset that comes from putting out fires, dealing with emergency and what others deem as most important.

Quadrant 2—Not Urgent and Important (value adding): Being pro-active about your health, well-being, relationships, time with family, exercise, planning. This leads to a disciplined, self-mastery life.

Quadrant 3—Urgent and Not Important (waste of time): Many of us put a lot of time here with activities that are not going to add any appreciable value to our lives or the lives of those around us.

Quadrant 4—Not Urgent and Not Important (counterproductive): Time wasters/busy work that demotivates.

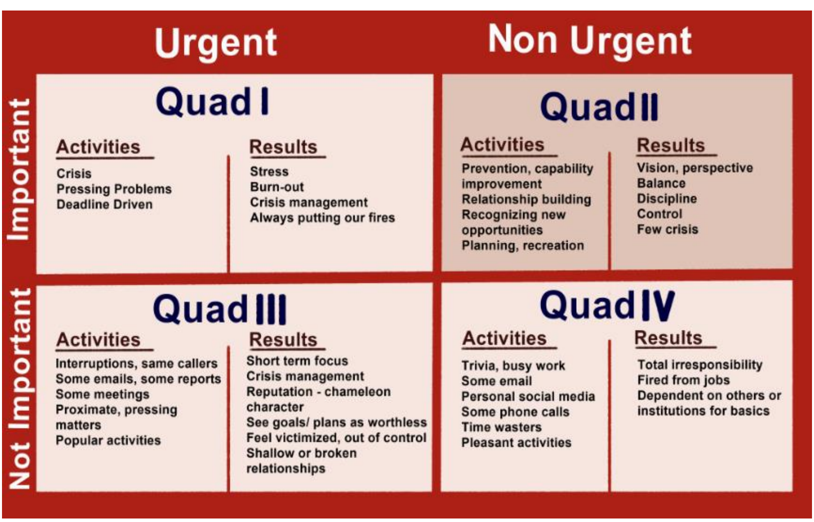
We may be surprised to see how little time we spend in Quadrant 2 activities. *Estimate the percentage of your time that you are presently putting into each quadrant on this chart:*



Effective people stay out of Quadrant 3 and 4 because, urgent or not, they are not important. They also shrink Quadrant 1 down by spending more time in Quadrant 2 (see below).

MANAGE Crisis and Pressing Problems

FOCUS on Strategies and Value



AVOID Interruptions and Busy Work

LIMIT the Trivial and Wasteful

What would it mean for you to spend less time in:

Quadrant 4?

____

Quadrant 3?

____

Quadrant 1?

____

____

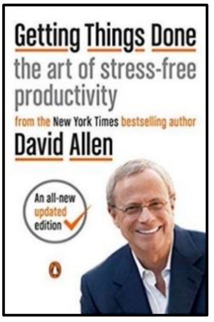
And more time in Quadrant 2?

____

____

____

Integrating Your Mission into Your Schedule



Now that you have a mission statement and are seeking to focus on what's important (via Quadrant 2), you want to see that priority focus show up in your actual day-to-day schedule. To do so I would recommend using/adapting David Allen's approach in his book, *Getting Things Done*.

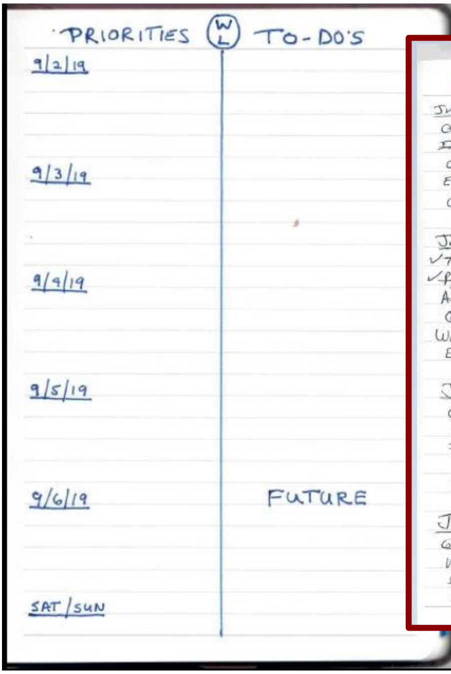
Allen encourages us to get everything out of our minds (to free up that space for creativity and vision) by putting the things we need to get done into an orderly means of accomplishment.

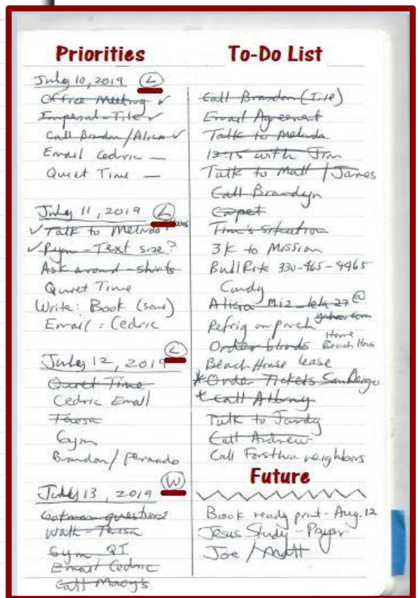
There are plenty of software apps (e. g. Evernote) and paper schedulers to help. I've used a combination of Samsung Notes (from an Android Galaxy Note) and a paper scheduling system which lists.

To-Do's >> Priorities >> Projects

I schedule weekly. Each day (often the night before) I determine my top five priorities (absolute musts) for that day from my to-do's. For incentive I also score the day before as a **W**—I'm a winner for completing all five or an **L** I'm a Loser for not. I certainly like W's more than L's!

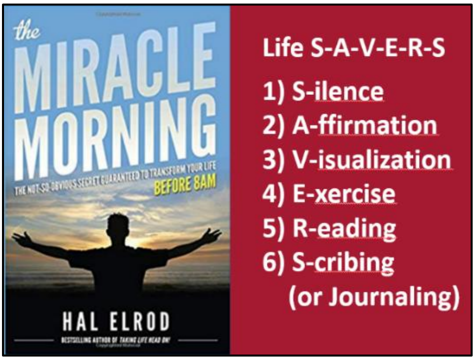
On another sheet I run a Projects List of my current five most important projects and "D them out:" *Do It / Defer It / Delegate It / Drop It*


PRIORITIES
TO-DO'S
9/2/19
9/3/19
9/4/19
9/5/19
9/6/19
FUTURE
SAT/SUN


Priorities
To-Do List
July 10, 2019
Quiet Time
July 11, 2019
Quiet Time
Write: Book
Email: Cedric
July 12, 2019
Cedric Email
Gym
July 13, 2019
Future
Book ready print - Aug. 12


TO-DO'S
PRIORITES
PROJETS
DO IT
DELEGATE IT
DEFER IT
DROP IT
9/2/19
9/3/19
9/4/19
9/5/19
9/6/19
SAT/SUN
FUTURE

Implementing Your Mission with Best Daily Practices



We've just outlined success in terms of establishing, reviewing and scheduling your life's top priorities. Winning our life starts with winning our day. Hal Elrod makes a great case for getting up early, yes before 8:00, to win your day by establishing six best practices.

Whether you're an early morning riser or a late-night person, you would do well to read his book, *The Miracle Morning*. Here Elrod distils best morning practices into an acronym he calls *LIFE S-A-V-E-R-S* which can be completed in six minutes or 60 minutes (see above).

His point is that a morning focus on what's important helps arrest our tendency to rush into our day doing mediocre things or what someone else has planned for us rather than the best life we can fashion. It's in the first few moments of the day that we can we best lift our self-confidence, enhance our health, boost our energy, challenge old paradigms, broaden our perspective and encourage creativity. All that is possible if we can create a consistent mind/body space for ourselves first thing each morning.

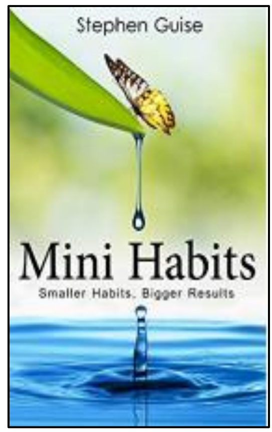
Beside reading the book, I'd suggest you carve out a special place to settle into. Mine is a comfortable, cushy rocking chair in our living room. This morning quiet time has become the well-spring of my life.

Elrod says that you can create a new habit in 30 days in three phases: Days 1-10: *It's Unbearable* / Days 11-20 *It's Uncomfortable* / Days 21-31 *You're Unstoppable*. Okay, yes but be careful of making huge pledges to establish new habits. Instead, consider…mini habits.

Master Ity, Bity, Tiny…Mini Habits

Often, we chart out large expectations for ourselves only to experience failure. So, what to do? Lower your expectations from reading 10 minutes a day to…one minutes or from reading 10 pages a day to one page. You still get something done and maybe, just maybe you stretch out that habit for a longer period and just can't help but continue.

A mini habit is a stupid small habit you can not fail. -Stephen Guise, author of Mini Habits: Smaller Habits, Bigger Results



Objects in motion stay in motion. Objects at rest stay at rest. Newton's first law also applies to human behavior. Just to start something, say exercising, often means we keep it up. But if we don't, well a minute will suffice. We'll take up our same mini habit again tomorrow with the same low expectation, small commitment and guilt-free gusto!

Starting something is often the biggest challenge we have when it comes to productivity. But once we start, we more easily carry on. If you have the desire to clean your desk, taking on the entire desk might be just too overwhelming. So, how about cleaning out one drawer? It's something, which is more than nothing, and you feel good about what you've accomplished—which is a critical part of keeping on.

So, forget the big goals and habits that trip you up and then eventually fall apart. Instead start a small habit with minimum effort. Read for one minute, do one push up, write one paragraph. Objects in motion, stay in motion. Motivation often continues after starting. So, start out small!

What old habit(s) do you want to stop?

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What new habit(s) do you want to start?

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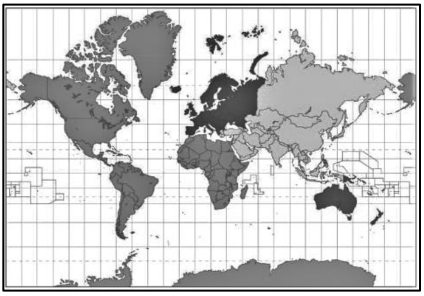
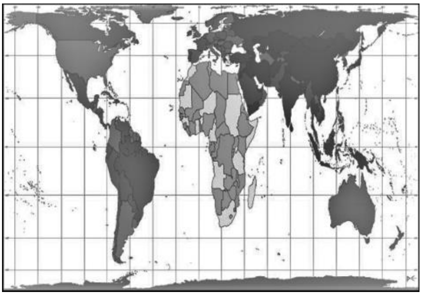
AND beyond New Healthy Habits, be open to Paradigm Shifts

A paradigm: *The way an individual perceives, understands, and interprets the surrounding world; a mental map.*

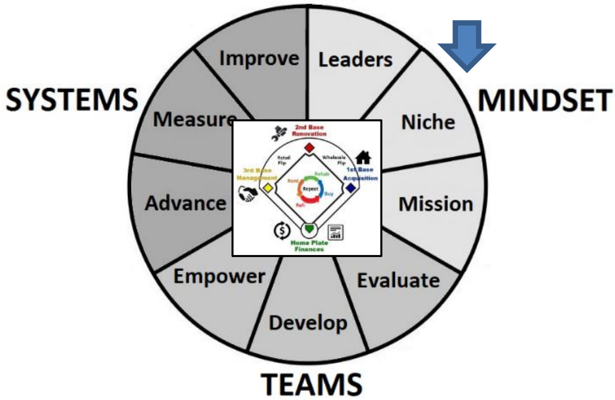
It is difficult to display a sphere on a flat surface, but when you do which map below are you most use to? Now, which map do you expect is more accurate—the familiar Mercator Map, created in 1569, or the Peters Map created by a computer, square mile by square mile? The Peter's Map offers a new paradigm to literally view the world.





Does it matter how you perceive you world? Almost every significant breakthrough in science (and every other area of human activity) is first a break with tradition, old ways of thinking or old paradigms. Adopting a new paradigm(s) is the best way to 10-xing your life.

If you want to small changes, work on your behaviors; if you want quantum-leap changes, work on your paradigms. –Steven Covey



CHAPTER 12 / Step 2

MINDSET: Niche-Focus breeds expertise

You are probably not an expert in Toyota trucks built between 1979-81. I (Bill) am, or at least I was back in the early '80's.

My parents gave me and my wife a second car, a red 1976 Ford Granada with a black vinyl top no less! I called it Battlecar Galactica and couldn't wait to get rid of it. But what was I to replace it with?

I didn't want to buy new (don't get me going on depreciating items again) and I wanted a truck, so I determined that a Toyota from the years 1979-81 was old enough to get it for a good price and yet still a very dependable vehicle. So, I spent time researching what I wanted, how much they were worth and where I could find one.

To help my search I paid for a classified ad:

Wanted: 1979-1981 Toyota pickup.
Will trade for Ford Granda and cash.
Call Bill at 541 XXX-XXXX

Gary from Corvallis called to let me know he had a blue 1980 long-bed, ¾ ton Toyota pickup with a canopy. He needed to reduce his payments to qualify for a house purchase and yet still needed a car for transportation. Perfect. We made a deal that included $2,000 more from me and we both went away happy.

My expertise might not have been wide, but it was deep. I knew virtually nothing about other makes or years of vehicles. But I was the master of the ’79-81 Toyota Pickup truck niche, the undisputed expert, no, niche-pert! And that truck ended up being my primary ride for 17 years.

Your “Hedgehog Concept” (simplicity within the three circles)

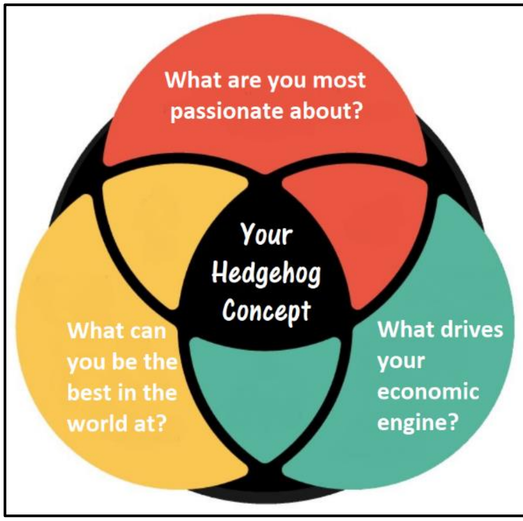
Being the world’s expert, as I was briefly with ’79-’81 Toyota pickup values, or in Jim Collins’ terms, “the best in the world” is one of his three circles that make up our Hedgehog Concept. The other two have to do with passion and getting paid.

To explain this concept let’s look at the difference between a fox and a hedgehog that Collin cites from an essay by Isaiah Berlin. A fox is a very clever creature. It sees the world in all its complexity and can pursue many goals at once. A hedgehog is a much simpler creature. It doesn’t get bogged down by all the complexity.

Hedgehogs are only able to do one thing well—curl up into a ball to protect itself. They are not capable of seeing complication or intricacies. All they see is a single goal and they execute to achieve that goal.

Good to Great companies, according to Collins, behave like a hedgehog. They stick to doing what they’re best at and avoid getting distracted. Getting distracted, I think, we’d all acknowledge that is incredibly easy to do in business, with even the best of companies having to fight to stop this from happening.

So, how does your real estate organization become more like a hedgehog and less like a fox? You can find your Hedgehog Concept at the intersection of these three questions adapted from Jim Collins:



1. What do you feel most passionate about?
This is a very important question because passion is hugely motivate-ing. Great don't tell their employees what to be passionate about. They find what they are already passionate about and look for the job description/projects aligned to those passions.

2. What can you be best in the world at?
This is far more than developing core competency. It's about deciding on a KEY NIHCE that your business can do better than any other business. It's then about focusing on this niche so nobody else can match your ability in your area. And note that this is about focusing on what you ***can*** be the best at, not what you ***want*** to be the best at.

3. What drives your economic engine?
You think of the economic engine like the blood flowing through our bodies. It doesn't define who we are, but we need it to survive and to thrive in accomplishing our real mission of providing value for those we serve! What are the most important factors and uses of your time that creates equity and cash flow for your business?

If our business is working at the intersection of all three issues: *Taping into our passion/Doing what we're great at/And make money doing it*, we've found the *Good to Great formula*.

I'd encourage you to read Collins' book. He identifies how this Good to Great formula addresses startup businesses while other books he's written, especially, *Built To Last*, looks at well-run companies that have stood the test of time and been operating for over 50 years.

Good to Great companies set their goals based on their Hedgehog Concept. This is very different from setting your goals on a desire to make money or to grow. It's all about a passionate mission that can financially feed itself to keep growing and spreading its influence in to those who need its services.

Your hedgehog concept will take time to develop. It's not going to happen overnight, in a flash of brilliant inspiration. To help develop their Hedgehog Concept many companies use what Collins calls a *Business Council*. A business council is a group of people from different areas of a company who meet regularly. They are tasked with finding their Hedgehog Concept and, once found, ensuring it is being ruthlessly driven forward.

Operating with a "Business Council"

Of course, when the company is relatively small its key leader may be the only business council representative, as I (Bill) was for years. However, even at this stage of your business' life you will want to reach out to a respected group of business people in your network to take on an informal role for guidance as your company grows.

Wherever your business currently is at, who fills these roles for you? How often and in what ways do you access their help and perspective?

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As the company develops, key individuals, especially those inside, take on that keeping-you-on-track/growing the vision role. At this point in the life of our company we have formalized five others who provide such ongoing direction. We call us the *E-Team* (Executive Team):

1) **Bill Syrios:** Stewardship's Founder
2) **Amanda Perkins:** Operations Manager
3) **Andrew Syrios:** Kansas City partner
4) **Phillip Syrios:** Kansas City partner
5) **Ryan Dossey:** Indianapolis partner
6) **Rebecca Horton:** Lender Relations

Our E-Team meets weekly via Zoom to talk over major issues such as proposed property purchases submitted by partners, current cash reserves, major hiring decisions, etc. We want to take advantage of great opportunities and be careful of making mistakes. The E-team members help keep us focused on growing our businesses within the confluence of our passion/competence/profitability:

Stewardship's Hedgehog Concept:

Finance and purchase under-market properties to efficiently renovate and manage well for increased equity and cash flow. Keep the best and flip the rest to help fund our primarily buy and hold operation.

Niche Thinking help you avoid distractions

In the second year of discovering a lucrative student housing niche (which I'll talk in-depth about momentarily) I made a big mistake. I came across a small street of houses for sale in the small town of Dexter, Oregon about 20 minutes away and pulled the trigger. They needed a lot of work, but the owner was willing to seller-finance, so I purchased them in a packaged deal. As it turned out I did relatively well financially. But it was a bad deal because I lost a year of momentum in my primary, more lucrative student housing niche.

Even worse, in the spirit of "multiple streams of income," a decade later I bought a trucking business operating five belly-dumps and a couple of flat-beds. I'll bet you can see where this is going! This time I did lose money and I also lost something more precious, my focus.

As it turned out this ill-advised venture pretty much violated each of the three criteria for me: I wasn't passionate about trucking, I had zero competence in running such an operation and yes, surprisingly, it turned out to be less than profitable! All in all, it became a huge distraction for the better course of a year.

If the E-Team (or even its informal equivalent) would have existed I dare say I would have had some individuals telling me, no yelling at me: "DO NOT DO THIS THING!"

Entrepreneurs, by nature, can become bored ("Oh, it's just another property purchase, so very dull and uninteresting") and, as a result, stray by falling for the shiny object syndrome. Our inner circle (business council, E-Team, whatever) often will perceive things we don't and can help you stay focused. They could have spared me from what my conclusion about the trucking: Belly dumps are not all that shiny!

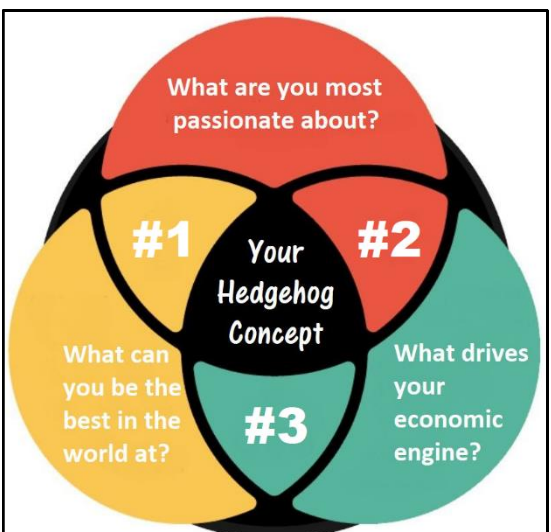
Every time we say "yes" to something we simultaneously say "no" to something else—often without seriously considering the value of that something else. There will come a time to "broaden out" our initial niche focus but with well thought through intention. Even the ultimate multi-niched company, Amazon.com, started with one very niched concentration: selling books online. Jeff Bezos' dream was always much larger in scope, but he went deep to test his strategies, fine tune his methods, establish his financial foundation, before going wide.

I have a friend who interrupted his real estate investing to attend law school, then to practice law for a few years. Suffice to say he later went back to real estate and is now a recovering attorney (his words). Granted this could be a great plan if you have a God-given talent and burning desire for lawyering. But for my friend it was a financial step backward because he spent years gaining the kind of expertise (and spending lots of money to do so) he can now hire and would otherwise be years ahead in building his real estate portfolio and skillset.

Another friend has a daughter with an uncanny knack for real estate acquisition starting when she was thirteen years old. (She finds the properties online, even calls and negotiates deals. Then her parents take it from there.) Should she follow the "normal path" after high school and go to college? That's not a bad use of her time but the good is so often the enemy of the best. Why not use those years to fine-tune her skills by continuing to earn her PhD from the University of Real Estate Investment and do things in her twenties that most real estate investors don't dream of doing until their forties or later!

The Good is the Enemy of the Great

My misguided trucking venture was a no-brainer, falling short on all three out of three questions! But there are other times that we are ever so close to our hedgehog concept, maybe even hitting two out of three, but still failing because we end up settling for something good and not something great…and yes, the good is always the enemy of the great. Let's look at three areas outside of our hedgehog concept.



#1. You like it, you are good at it, but it does not pay or pay well. This is a hobby and better left for free time.

#2. You like it, it pays well but you can't be great at it. This is a recipe for mediocrity.

#3. You're good at it, it pays well but you don't really like it. Welcome to the classic burnout!

Remember the Toyota story? My lack of trucking expertise stands in sharp contrast to my passion and expertise, albeit brief, for ’79-’81 Toyota pickup trucks. With that specific niche, I killed it!

If you can adopt this same kind of niche-focus to a lucrative area of real estate, it will likely make you wealthy because the riches are in the niches. I built a variable fortune on one real estate niche, student housing around the University of Oregon in Eugene and later, used this financial foundation on which to build many other real estate investment niches and partnerships.

The Student Housing Niche

By the early ‘90’s I had become an expert in student housing. This was a natural for me since I had been a campus pastor. I liked students and I knew what students liked. When I melded my knowledge of students to real estate investment, I quickly discovered a value-add feature unique to this niche:

Creating additional rental income by increasing the number of bedrooms (and secondarily) bathrooms in campus rental properties.

Hang in there while I get deep into the weeds about student housing. I do so to illustrate the value of finding and focusing on your hedgehog concept. By focusing on a niche market, you will discover things unknown to others and with this specialized knowledge create a great opportunity as you will see.

It’s All About the Bedroom

When students look at a house they see right past the nice lawn, beautiful fireplace, tiled showers and crown molding. Those amenities are all well and good but what a student thinks about is where he or she will reside. Their place, even though they are renting with four of their friends, is their particular bedroom—their “home within the home”—and secondarily, their bathroom. After that they’ll think about where they'll hang out to make dinner, wash their clothes, watch TV, and yes, play beer pong.

Instead of thinking of a campus house like a typical rental, campus investors see it as a small apartment complex. The idea is not to rent houses as individual bedrooms but to the whole group. However each bedroom is, in effect, its own one-bedroom apartment unit. Our revenue per bedroom will be the determining factor of the property's potential value. If we can increase the number of bedrooms (and a correspondingly appropriate number of bathrooms), we can significantly increase the rental value of the property. This is a key value-add.

So, if you can create an extra bedroom in a basement, garage, large family room where there wasn't one before, you've just created "another apartment unit" and the corresponding increased revenue: of $400, $500 or $600 per month. If you can create two bedrooms, then double it: to $800, $1,000, or $1,200 per month. (As you go up in bedroom count, the rent per bedroom goes down slightly because a smaller house usually rents for more per bedroom than a larger house.)

Whatever the per bedroom rent amount is common in a particular campus market and in a particular proximity to that campus, another bedroom or two or three can add up to a lot of additional revenue that justifies rehab capital spent on the necessary upgrade.

If it cost you $20,000 to add an extra bedroom (or $40,000 to add two bedrooms, plus a bath for say another $7,500) what would that be worth it to you? If you receive an additional $450 per month, how long will it take you to pay off the amount of rehab capital it took to create the first bedroom? At 10% interest the extra $450 a month will pay off your $20,000 loan in five years with an extra $25 per month to spare. If you were able to finance this rehab your return would be infinite because you are using someone else's money to create $25 a month for five years and then $450 per month until the end of time (or even more when you raise the rent).

By adding $400-1,200 a month, a campus rental investor increases the property's value substantially, as much a $100,000 or more. Similar to multifamily, the value of student housing is tied to its income generating potential which is most appropriated gauged by Capitalization rates (CAP). (CAP rate = annual net operating INCOME after all expenses except mortgage / by the property's VALUE). There would be virtually no additional monthly operating expense for adding a bedroom. So, if CAP rates are 7.5%, an increase in annual income of $5,400 or $450 per month would (theoretically) equal an increased valuation of $72,000 (5,400 / .075 = 72,000), and if CAP rates are 6.5%, the (theoretical) increased valuation would be $83,076!

More bedrooms lead to increased cash flow and value.
Given the priority of THE BEDROOM, we keep living areas modest in size. Students can go to their friends' houses to party and that extra first-floor square footage can potentially be used to carve out another bedroom in an oversized living room—oops, I meant another $450-$650 a month in rent (and the corresponding value increase as well). Not all houses lend themselves to transforming say a formal dining room into a bedroom, but some will. Campus investors have eyes to see such value-add spaces.

Students view apartments similarly: What will their particular bedroom/bath include and, finally, the living space? Apartments do not usually provide the same opportunity for bedroom additions the way the houses can, but that isn't always the case. How about that large storage room? Could it be another unit? Is one of the larger units inefficiently laid out and with the potential of carving out a studio? I've turned a 27-unit campus building into a 29-unit by employing such an efficiency mindset. I always ask myself, "Is too much square footage given to something other than bedroom space?" and I always hope the answer is, "Yes!"

Changes I've Made to Create Bedrooms "Out of Thin Air"

--Transform a one bedroom side-by-side duplex to a five-bedroom, two-bath house by "putting it back together," taking the better of the two living rooms, the better of the two kitchens and rearranging the rest into the most functional floor plan possible.

--Create two bedrooms and a bath out of a two-car garage, converted carport or a large family room.

--Carve out an extra bedroom in a utility room and move walls to take out some room from the existing bedroom, fashioning two bedrooms out of one.

--Transform a dental office into a campus rental with small bedrooms granted. But remember, you can buy or build bunk/desk units for students which helps make up for the lack of floor space.

--Carve out a bedroom from a garage and leave the existing garage door with enough room in the front for bike storage.

--Dig out a low ceiling basement to change a large storage area into five bedrooms, a bath, washer/dryer area and small den. Yes, this was a huge project!

--Divide a very large bedroom into two bedrooms with a small hallway to get to the back bedroom.

--Add a bedroom above the garage that connected to the upstairs of the house.

--Use a large eave storage space to construct a cool, angular ceiling bedroom with a pocket door.

--Carve up a fraternity house into 11 apartments: one studio, two 1-bedrooms, one 2-bedroom, four-3 bedrooms, one-4 bedroom and two 5-bedrooms. Granted this took hundreds of thousands of rehab dollars but we substantially increased the number of bedrooms in this building by reorienting the apartments with a more efficient layout.

You can see why people have called me “Bedroom Bill.” My bedrooms have gone where no bedroom has gone before! To me this moniker simply spells ADDITIONAL CASH FLOW. Some now point to small closets enticing me to perform my magic bedroom appearing act. I say, “Don’t tempt me!” They know I’m open to any and all ideas when it comes to increasing cash flow by adding bedrooms and complimentary bathrooms.

In your “bedroom enthusiasm” be aware that many communities have city ordinances not allowing more than five unrelated adults to rent together. There are even a few cities that limit it to no more than three unrelated adults in certain residential areas. Our particular city allows a usage exception called “congregate living,” which permits renting to up to nine unrelated adult in certain, higher density areas. Check the particular ordinances in your city.

Meet Mark and Chris

Mark Pankalla started out by working for me and later partnered with me. Mark is a contractor or better put, a craftsman. While I was into quantity he was into quality, so our partnership was relatively short-lived. Mark went on to target homes on the fringe of the University of Oregon campus area that he could “cherry out” with beautiful wood floors, kitchen redesigns, skylights, and first-class landscaping. When a student steps into one of Mark’s places, they want to rent it, not for its prime campus location, but for its old-world charm.

This kind of niche within a niche works well for Mark as he has been able to increase rents with virtually no vacancy in the last twenty years. To date he has purchased and rehabbed or built new six beautiful campus homes and makes a solid monthly cash flow to supplement his contracting income.

Chris Francese was a University of Oregon business major who participated in an internship with nine other students I put on in the summer of 2005. Chris got on the inside of our company. For three months he immersed himself in marketing to sellers, negotiating, participating in rehab and property management. Apparently he liked what he saw because when he graduated and returned to his hometown in Poughkeepsie, New York, Chris didn't look for a job. Instead he kept his expenses at a minimum and went to work targeting properties close to Marist College, a private institution of about 6,300 students.

Chris now owns ten large campus rentals. He pretty much does it all—purchasing, rehab, maintenance, showings, you name it—but he recently began hiring out some of the work. What's wonderful about Chris' situation now is that not only can he live solely off his campus properties' income; he has extra travel money, one of his passions in life. (I follow his traveling exploits on facebook.)

Before you run out to target campus housing investment, there is much more to digest about this niche. I have a BiggerPockets podcast on the subject: *The Riches are in The Niches, Like Student Housing* (#140): www.youtube.com/watch?v=GArzKgkLrSE&t=2205s

Another Similar Niche: ADU's and "Condofying"

A comparable non-campus version of this niche is creating an accessory dwelling unit (ADU) in a basement, garage, family room, etc. to provide additional rental income. One of my partners found a beau-tyful two-story home with a large unfinished basement in northeast Portland. We first put in a washer/dryer on the main floor and rented out everything above the basement. In fact, it was the basement of the house that really got our attention with its high ceilings and a natural, separate side entrance. So, we then remodeled that space into an upscale apartment. While this cost us over $100,000, the rental increase was $1,600 a month.

Another friend splits lots one of the most desirable areas in Austin, TX (a very friendly in-fill community) which allows him to "condofy" the property and build up an additional 1100 sq. ft. house on the backside, off the alley that he can either sell independently or keep as an Airbnb.

Of course, you'll need to know city code requirements for such additional dwellings or ADU's but they can essentially transform a single family into two rentable or even sellable units (with restrictions). This is a powerful niche market that adds rental value thus increasing the actual sales value with relatively cheap square footage.

I've even built a new house with an ADU. New construction square footage is more expensive, but the benefit is that there nothing to retrofit. Either way, an ADU provides a unique niche rental product that is also very sellable. Some will use them for relatives, monthly rentals, or short-term Airbnb vacation rentals.

The Riches are in the Niches

Most people will never need neurosurgery, but when they do, no one else on the planet can help them including other physicians. It is this very narrow specialty that makes what neurosurgeons do so valuable and why they get paid so much more than general practitioners. Their highly specialized expertise makes them "niche practitioners." Of course, there is nothing wrong with being a family doctor. But because their service is generally available it is more of commodity than a specialty in the medical field.

The same holds true in businesses. Who offers the most value to the flying public? The airline pilot or the flight attendant? To answer that question, all one need do is look at the salaries of each. Again, it goes back to specialization and training. One can become a flight attendant with about six weeks of training while becoming an airline pilot takes years. Pilots are thus a much more niche position in the airline industry. And, of course, among pilots there are increasing levels of certify-cation until one becomes a captain, the most highly skilled and compensated of all.

All of this focus on specialization holds true for real estate investors as well: the more highly trained we become in a niche market, the more this specialty will pay off for us.

Real estate niches include an interlinked combination of four factors:

PROPERTY TYPE / DEAL SOURCE / END-USER USE / SPECIFIC LOCATION

PROPERTY TYPE: Each type of property presents its own prospects as well as challenges. Many investors start with single-family and later move into other specialties as opportunities arise.

Single-Family Homes • Condos • Duplexes/Triplexes/Fourplexes • Small Apartments • Large Apartments Communities • Manufactured Homes • Manufactured Parks • Commercial (Office) • Commercial (Industrial) • Commercial (Retail) • Self-Storage • R/V Parks • Undeveloped Land • Lots • New Construction

DEAL SOURCE: Investors are problem solvers for people who find themselves in life situations prompting them to sell. These situations act as small niches unto themselves and sources of deals to which we can specifically market.

Pre-forclosures • Short Sales • Foreclosure Auctions • REO (Bank Owned) • Bankruptcy • Tired Landlords • Probate • Divorce • Tax Differed • Divorced • Code Violations • Fire Damaged

END-USER USE: Every business has a niche customer base and ours can include buyers, tenants, and other investors who compensate us for product or serve our financing needs as lenders.

Flipping (Wholesale) • Flipping (Retail) • Flipping (Luxury Homes) • Lease/Option • Longer-Term Rentals • Short-Term Rentals (Weekly/Monthly or Airbnb) • Vacation Rentals • Student Rentals • Section 8 & HUD Housing • Special Needs Groups • Tax Liens • Real Estate Notes • Hard Money Lenders • Other Private Lenders

SPECIFIC LOCATION: Most investors start out close to home while some are more strategic when it comes to location. Strong cash flow will usually necessitate investing in less affluent neighborhoods. Buying in the “path of progress” could make a substantial difference when it comes to appreciation and, of course, who isn't looking to buy the worst house on the block!

Country > Region > State > City > Zip Code > Neighborhood > School District > Block > Property

The Value Focus: On lower/middle/higher end properties for flips or on particular rent-to-cost ratio targets for buy and hold rentals.

NICHING DOWN helps you focus on what's important

A niche is a specialize corner of the market that can become highly profitable as we focus on it, market to it, coach-up teams and implement systems within it.

Our goal is not to be generalists but "nichists." Niching down will help us to specialize and gain the needed expertise to turn our cookie cutter stamp into a machine. It also defines our competition, brings us clarity regarding our priorities and the use of our marketing dollars as well as directing us to other like-minded investors to network and continue our education.

For illustration purposes, let's niche-down my campus rental focus:

Purchasing and rehabbing single-family homes (property type niche) in the outer rim of campus housing where they were less expensive (niche down), that had the potential for increasing bedrooms without adding new square footage (niched down again) by marketing to sellers who are unaware of the value add potential (deal source niche) of student rentals (end-user niche), especially sophomores and juniors (niche down again) in Eugene and Corvallis, OR (city niche) around the University of Oregon and Oregon State (neighborhood niche).

In a nutshell this niche has been: *Purchasing properties for University of Oregon and Oregon State University student renters that were somewhat beyond the most desirable campus locations that, when possible, could affordably add bedrooms (and bathrooms) for increased cash flow and equity (in order to refinance and expand).*

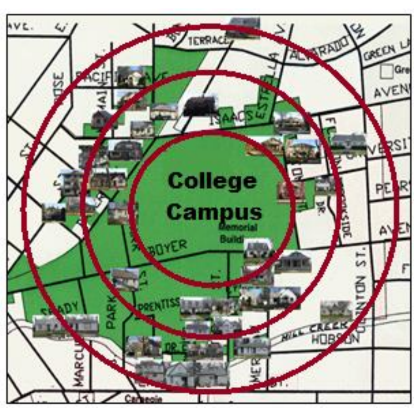
Niching Down Further: Proximity to Campus

The statement above is an example of "niching down" your thinking. As a campus investor, you care about what students care about. Students don't think about manicured lawns or two-car garages or any garage for that matter. They don't care about being located near the best schools. Their community is within their campus network.

Location to "their world," the campus, rules the day for what students deem to be the most desirable place to call home. They look for convenience to classes and to other student services which translates into proximity to campus—the closer, the higher the demand, and the less the supply, and thus the highest rents and the lowest vacancies.

Because the one thing you cannot move is the property itself, location is always important. Properties are usually rated by their age and amenities. These are important factors for campus properties as well, but the overriding factor is location to campus. Students love convenience. Who doesn't?! So, walking distance to campus is best, biking second and driving last. Here's how students "grade" rental locations:

A: a few blocks away—
walking distance
B: ½ mile out—
walking/biking distance
C: 1-2 miles—
biking/driving distance
D: beyond 2 miles—
driving distance
F: just too far away—
a "different area of town"



Certain sides of any given campus are more desirable than others. Is the west side the preferable one or is the south side more desirable? Interview students for their opinion but, at the same time, realize the most desirable side might not be the most profitable side. “A-campus properties,” and secondarily “B-campus properties,” demand more rent, lease more quickly and are nearly never vacant. However, they are also the most expensive to purchase, sometimes much more so.

So, should you go after A, B, C or D located properties? It’s a good question. How do you identify the “sweet spot” in order to purchase and manage student rentals for their best return on investment (ROI)?

Consider targeting the sides of campus that are less expensive and buying a little further from campus than walking distance. In doing so you will have lower rents but often dramatically lower purchase prices that more than compensate for those lower rents. So while an A or B location brings better rents, C and D locations can bring much lower purchase prices and yet, may not devalue the rents a commensurate amount. They would thus end up being better overall deals.

NICHING UP helps follow new, profitable opportunities

Niching down helped me build a solid financial base from student rentals. I’ll spare you the details, but this first niche gave me the means to “niche up” and create many more, opportunities primarily with a group of younger partners spread throughout the country as follows:

Jim: Our partnership began with securing redemption rights to properties in judicial foreclosure with a six-month right of redemption (a highly-niched market), and then renting them out before foreclosure while seeking to do short sales with banks. It has grown from there to include general buying of undervalued properties throughout the Portland metro area down to Salem.

Tori: Is currently my key acquisition manager in Lane County: Junction City to Eugene/Springfield to Cottage Grove, OR. She heads up a team that locates single family to fourplex properties through foreclosure auctions, short sales and pretty well anywhere else she can find them.

Andrew & Phillip: My two middle sons moved to Kansas City in 2011 where we have purchased, rehabbed and manage an extensive portfolio of both houses and small apartment buildings. They helped us focus on the Midwest as a cash flow region.

Patricia: We partnered in 2015 and own an adult recreation and wellness center that Patricia oversees in a commercial building owned by me and sons in Kansas City. This kills two birds with one stone: keeping our place rented and participating in a successful business.

Ryan: Having moved to Indianapolis for his wife to study for her PhD, Ryan turned to real estate investing. He became a direct-to-seller marketing guru but was only wholesaling the properties he found. Our partnership, focusing on both single families and apartment buildings, allows Ryan to do buy and hold investing and gives Stewardship yet another cash-flow market.

Kyle & Jessica: My nephew and niece partner with me in Emporia, Kansas (where the Harvard of the Midwest, Emporia State University, quietly goes about educating young minds like mine at one time). Kyle is building a fast-growing real estate investment company, thus far focused on single family, small apartments and retail commercial.

Greg: We first partnered in 1993 to buy an apartment complex in Eugene with great success. In 2011 Greg moved to Texas where we have focused on larger multifamily properties, and more recently, we added a partner, Jay, to buy single families in the Dallas metro area.

Sandor: We have purchased bank paper all across the country and have owned 100 non-performing 2nd's behind performing 1st's. While their lenders failed and sold off these 2nd mortgages, our company works out discounted payoffs and payment plans with homeowners.

Matt: With a degree in architecture and an extensive background in building homes, Matt joined our team in January of 2016 to head up our new construction division. We now own a number of lots and have become primarily build-to-rent investors in our local community.

Amanda: Clearly, we have a lot to manage, and Amanda's capability as our operations manager has allowed us to expand in ways not otherwise possible. Our entire operation, currently in five states, reports to her. Amanda and I are also partners with Jim in Portland.

These partners/key staff are skilled investors. They focus on key niche markets in diverse geographical areas with office and field teams they have trained. Their unique strengths and practical expertise have brought great wealth-building opportunities to our company, not to mention keeping me engaged and younger than my age would ordinarily warrant!

Going All In

Now for one more question: Are you full-time? Maybe you've already made this decision (and "going full-time" now has more of an attitudinal meaning to you), or maybe you're anticipating it in a year, or maybe you can't envision it at all? For many of us, it's a big step to walk away from a steady income and pursue real estate investment full-time.

A lot of factors must be weighed: spouses and family members consulted, the downsizing of current expenditures considered, along with the ramifications of loss of verifiable W-2 income with lenders.

There's no denying just how challenging taking this step has been for those who have done so and for those contemplating it. But if building a real estate empire is our goal, the step of going full-time is a no-brainer. The longer we put it off, the longer it will take for us to give our undivided attention to making that empire into a reality.

One of my partners who has experienced a solid amount of real estate success walked from a steady, six-figure salary. This has been no easy decision for his family, but they see the long-term gain outweighing the shorter-term pain. His statement to me: *Bill, I've stripped away all unnecessary expenses. I've formed a bare-bones budget to support my family. I set the date and didn't look back. I'm all in.*

Wherever you're at right now in the growth of your own real estate empire, what is the next step to take that indicates you are willing to go…all in?!

APPLICATION TO YOUR REAL ESTATE INVESTMENT BUSINESS

CHAPTER 12: Niche-Thinking breeds expertise

What niche real estate market(s) are you currently invested?

____

What is your most lucrative one(s)?

____

In 1834 John Jacob Astor identified the niche he would have liked to have invested in more (see p. 16) as the island of Manhattan. Fill in the blank from his quote identifying the niche you knew something about a few years back but didn't invest in but now wish you had:
If I could begin life again, knowing what I now know, and had money to invest, I would:

____.

The only reason to play the coulda, woulda, shoulda game is to change things going forward. Now, look as best you can into the future and identify the niche that you could conceivably invest in, and if you do, it may very well prove to extremely lucrative a few years from now: Since this is the first day of the rest of my investing life, I would like to invest in:

____.

What are the benefits/obstacles of investing in this niche market? What's your next step?

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Of the things on your Stop Doing List what will be the most difficult to give up?

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What would it mean for you right now to "go all in"? What are the benefits and challenges?

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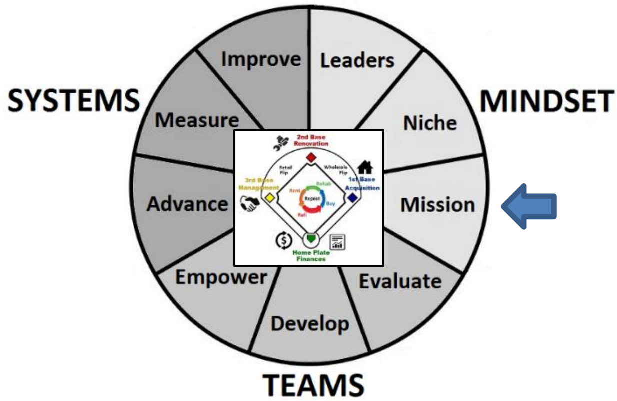


CHAPTER 13 / Step 3

MINDSET: Mission-Mindedness sets priorities

Some businesses exist to make money. That's the beginning and end of their mission. But creating a culture of passionate discipline gets short-changed with such a mindset. Money is to business what oxygen is to our body. If we don't have it, we will die. Likewise, if a business fails to make a profit, it too will falter and fail. But do we live for oxygen, or do we appreciate the fact that oxygen allows us to live?

The businesses most likely not just to succeed but to thrive focus on the bottom-line as a means of fulfilling what money can never buy: *the opportunity to leave their unique mark on the world.*

The owners of these businesses carefully manage an infectious, results-oriented corporate culture where their staff buy into what money can't buy. Making money is not the mission after all; it allows the mission to take shape and flourish.

Making Money Is Not a Good Enough Mission

Think of a passion or a cause you have been committed to (maybe it's an invention, an endeavor, a spiritual purpose, a family commitment, a non-profit or a money-making enterprise). How much could we pay you to stop doing "this thing" that you gets you up in the morning thinking about it and puts you to bed at night with it on your mind?

There might be a number to buy you off, maybe $1,000, $10,000, $100,000, $1,000,000, $10,000,000 or more. But if the passion is strong enough, the cause great enough, no price could buy you off. Even if your idea doesn't succeed or your efforts don't gain traction, money is a secondary consideration.

Start with your Most Important Asset: You

Your mission starts…with your passion expressed through your strengths. As a leader, what is your greatest contribution? What are your natural abilities and what strengths are lacking? (Some might call these weaknesses but they're just lesser strengths, right!)

Now, don't worry about improving what you lack. That might sound counterintuitive. If so, it is meant to be. There's a lot of research that shows highly productive people work to develop their greatest abilities only—giving no energy to shoring up weakness.

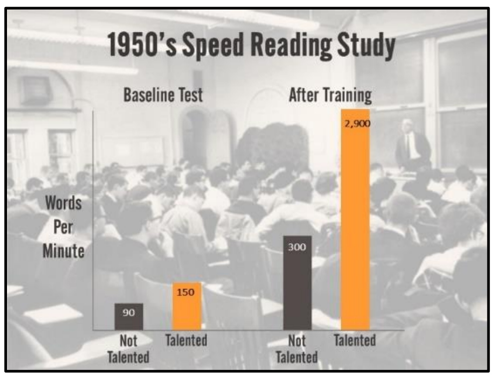
For those who remember Michael Jordan's baseball career, I rest my case! Now, if you'd appreciate a little more detail here, consider a research project cited by the Strengths Coaches of the Gallup organization.

In the 1950's, the head of a school in Nebraska prompted the state into running a test to determine the best way to teach students to read as fast as possible while retaining at least 80% of the content they read. The methodology focused on 10th grade students and started with a baseline test of how fast they read.

The researchers found that most students read at about 90 words a minute (not quite half a page in the average book) while retaining 80% of what they read. But there were a group of fast readers who could read an average of 150 words per minute and still retain 80%.

They put both groups of students through a six-week intensive course of speed reading and tested them again to see the results. The thought was that those reading faster would improve slightly but not to the extent that the average readers would improve. Some even predicted that the fast readers would experience a melt-down once they realized that they were performing at a higher level and that their speed would suffer.

The actual findings stunned the researchers. After six weeks the students who were reading at 90 words a minute increased their speed to 300 words per minute, an impressive 66% increase. But the students who had been reading at 150 words per minute increased their speed to a whopping 2,900 words per minute, an 866% gain and a lightning fast ten pages per minute while still retaining 80% of what they read.



This test has been replicated several times with similar results and a similar conclusion: People are vastly more productive, motivated and happy when their work lines up with their natural talents. We are wired—neuro pathways in our brain are formed before adult-hood—with a certain, unique network of synaptic connections. The strong connections get stronger as we age and the weaker ones wither. Ultimately, our brain creates a freeway of productively that shapes who we are with a bunch of little side roads that don't amount to much.

The Gallup Clifton StrengthsFinder assessment is a well-known skills test. Take advantage of this research! It identifies 34 talents in order for every person (go to StrengthsFinder.com). These talents occur in sequence, revealing your highest strengths or most dominate talents then progressing down as your strengths diminish. The data in the hands of strengths coaches encourages you to focus on your top five.

The order of your first five strengths puts you in a class all of your own. Out of the roughly 7.4 billion people in the world less than 225 have the same top five strengths in the same sequence as you. The statistics get really nuts when you match the top eight strengths: about 1 in 700 billion. As far as lining all 34 up, well, suffice to say, you have an absolutely unique set of strengths. No one who has ever lived on this planet or whoever will live, is the same as you!

There are far-reaching implications here but let me draw out some workplace ramifications. When an employee lacks natural ability in a certain area it is counterproductive to tell them to “work on it.” Spending time on weaknesses is a recipe for “focusing on the path of *most* resistance.”

Instead, get to know them for their unique talent-set: what they naturally take to, feel confidence in, have a good attitude about, or are driven to do? Can you match up what you need to have happen with what they are naturally motivated to do? If you can’t, they will need to find other employment, but if there is a match, you are giving that person the chance to magnify their nature talents and excel within their strengths.

To be sure raw talent can be used in a destructive, counterfeit, even evil way. Think of the Trojan horse that first appeared to be a gift only to end up as a means of destruction. Raw talent can also be left in idle mode and never become a force with which to be reckon. To reach its potential, talent must be tempered and melded with humility, knowledge, practice, skill, wisdom and experience before it becomes a genuine strength. Then natural talent becomes a beneficial and productive gift to yourself and to others.

Here's their Strengths' Equation from Tim Rath:

Talent: a natural way of thinking, feeling or behaving for you
x Investment: time spent practicing, developing your skill and building your knowledge base
= Strength: the ability to provide near perfect performance

Now what about you? What are you good at or drawn to? What do you stay up late at night thinking about and working on? Take time to figure it out because mediocrity awaits those who work on their weaknesses while excellence and greatness—the potential 866% productivity increase type of extraordinariness—comes to those who focus the majority of their time and energy on what they are naturally good at.

You cannot be anything you want to be—but you can be a lot more of who you already are! -Tom Rath, StrengthsFinder 2.0

What about your lack of strengths, your weaknesses if you will? Figure these out too. As you do, find the best ways to compensate for them: hire for them, contract out for them. If you're not an accountant type don't worry about anything more than the basics of bookkeeping (what's a profit and what's a loss!), same with construction, same with marketing, same with legal issues, same with design, same with property management.

This doesn't mean that your organization doesn't have to excel in the basics of real estate investment. It assuredly and absolutely must! (We highlighted those as four bases in the first half of this book.) But there are ways to grow your company by "covering the bases" without getting a personality transplant or turning your skillset into a pretzel and trying to be someone you're not.

A lot of what it takes to be a great business leader is *compensation*, not the money kind but the making-up-for-what-you-lack kind. Knowing you don't have the ability, not to mention the time, to get done all the critical tasks and yet finding those naturally talented people who, given the above equation, gives your organization a chance to excel through bringing their strengths into the mix.

I remember in the early days showing a home to a couple that I was selling (flipping would imply I was making a profit). As they came down from upstairs they commented, “We really like the house but the wall texture, what happened!?” I think I responded, “You just can’t find good help these days,” as I quietly committed myself to never texture another wall.

At that same house I glued on the kitchen countertop, only to realize it had a big bubble forming between the laminate and the fiberboard base. In my consternation I ran outside to find the heaviest, flattest rock I could. I sat on countertop on top of the rock for a good long while in the construction meditation pose and then left the rock there overnight hoping the laminate would stick. Now this might surprise you but I’ve never been asked to provide mentoring for my many such creative construction techniques!

Face it: we just don’t have the time, energy or inclination to be the jack of all trades. If we try, we will seal our fate as the master of none. So, know yourself, learn what you’re good at/like to do and get better at that while at the same time compensate for yourself with finding the best people you can as employees in your business and as outside specialists, contractors and experts who encircle your business to help it steadily and successfully grow.

To help envision such growth we’ll reference a number of business owners in the remaining chapters of this book who have “been there and done that.” We’ll evaluate both well-run midsize and large organizations to uncover what they did at various stages of growth and the principles behind their success and then apply these principles to building a real estate investment company, your real estate investment company.

After all, every successful company, including well-known Fortune 100 ones—Apple, Walmart, Southwest, Intel, Starbucks, Amazon, Nike, Walgreens, Kimberly-Clark, Google, Charles Schwab— started out where I started, where you started: one person with the determination to follow their dream. Why couldn't the next real estate investment equivalent of Amazon, Southwest Airlines or Nike start with us?

Every extraordinary enterprise began with the same, ordinary starting point: one person with a dream and determination. That person is YOU. You hold the key to your company's potential and to its pitfalls. You are, after all, a truly unique individual with great strengths but also one that needs others to compensate for what you lack in both talent and time.

Growth in excellence never happens in a vacuum. As we discussed in chapter 11, there is no way to create excellence around us without working on creating it within us. Most people live a life of "settling." They think about what they want to do, what they could do, what they see themselves doing but then they fall back into what they *are doing* and that amounts to a heap of mediocrity: time wasting activities, an undisciplined and unfocused lifestyle often full of excuses and blame shifting.

Are you ready to extract all the value you can from yourself as your company's greatest asset and compensate as much as possible for your liabilities by developing a great team? If so, consider an in-depth evaluation using the questions below. So, how will you:

Understand, develop and draw on your own strengths?
Compensate for what you lack through the strengths of others?

What are your strengths and how do they relate to real estate investment? (Feel free to stimulate your thinking by taking the Clifton StrengthsFinder assessment.)

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What are you doing to develop and use your unique strengths to build your company?

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What strengths do you lack that relates to building a real estate investment business?

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How are you/could you be compensating for what you lack to reach your goals?

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Hire Volunteers!

Great enterprises treat their employees as "volunteers." Clock-punchers get paid for their time to do what is expected, but only volunteers give away their mind and heart in the form of unexpected vision, desire, creativity and effort.

And what are such dedicated volunteers looking for in return?

STRENGTHS BASED: Volunteers only give their mind and heart if they know their opinion matters and contributions appreciated. And, whether they fully understand it or not, they want to work under those who recognize their strengths and who incorporate them within your organization using those particular strengths. This is the number one way to keep your best people engaged: play to their strengths!

But it goes one step further. Some people are strong at something but unhappy actually doing it. Their talent and their passion just don't line up. So instead of being energized, that activity drains them. Having a strength means being both great at something (or having the potential to be so) AND being happy doing that something. You're looking to empower people to become stronger and stronger within their natural strengths. (For more on this, check out *Now, Discover Your Strengths* by Marcus Buckingham and Donald Clifton.)

GREAT PEOPLE: Since we often spend more time "hanging out" with co-workers than family members, there is a deep need for mutual respect and even friendship within an organization's culture. Feeling valued, liked and appreciated as a team member makes all the difference. While it is not appropriate to routinely bring outside drama into the workplace, people want to be known and appreciated for who they are as a person, husband, wife, etc. not just what they can do to enhance the bottom-line.

But talented people need more. There is almost nothing as demotivating for an A-Player than to have to work around C and even B-Players who suck energy out of the workplace. It's like living in an apartment unit with a loud and obnoxious next-door neighbor. They'd prefer to stay put, but they just might move on to a better opportunity with higher quality teammates. The best thing we can do for our best people is see to it that their co-workers match the quality of what they bring to the organization. (We'll get back to this.)

SUPPORTIVE LEADERSHIP: Does the owner/boss/management have my back? Are they willing to take the blame when appropriate (or even when not) and share the recognition when appropriate (or even when not)? Is it clear that this endeavor isn't about them but about the cause, the mission? Is it evident this is about us and about me, how they can help me do the best job I can, grow in competency and realize my greatest potential?

For our strong people to excel, they need more clear and consistent expectations. A-players don't need hovering managers telling them how to do they're job. Instead they want coaches who help them know what is expected and who can give them tools of implement-tation. They particularly excel under an ongoing one-on-one coaching style that regularly identifies shorter-term performance goals and provides evaluation in the context of longer-term priorities.

APPRECIATIVE RECOGNITION:

Criticism is futile because it puts a person on the defensive and usually makes him strive to justify himself. Criticism is dangerous, because it wounds a person's precious pride, hurts his sense of importance, and arouses resentment. - Dale Carnegie

In Chapter 1 of his famous book *How to Win Friends and Influence People*, Dale Carnegie lays out Principle #1: Don't criticize, contemn or complain. While his words and illustrations, including some from Abraham Lincoln, are certainly inspirational, a business leader is left wondering how he or she could ever effectively critique subordinates' actions, behaviors and attitudes that need to change. One aspect of genius in Mr. Carnegie's book is that you must read it in its entirety before he gets back to answering that question.

What Carnegie describes in the 173 pages between his first chapter and his last one is how important it is to learn to like people, to be genuinely interested in them, to give sincere and honest appreciation, to smile, to use their name, to avoid arguments, to be a good listener, to make them feel important, to show respect, to be friendly, to let them do the majority of the talking, to make sure they get the praise, to show deference to their ideas and on and on.

Finally, then, in his last chapter, *How to Change People Without Giving Offense or Arousing Resentment*, Carnegie lays out nine principles beginning, "If you must find fault, begin this way…" His book is a virtual must read for every (aspiring) business leader who wants to promote a positive, appreciative corporate culture, the very culture necessary to build a winning team with a winning attitude. That culture begins with us, and our commitment to its importance.

IMPORTANT WORK: In the right strengths-based context and positive, results-oriented culture people thrive because they believe in the mission that sees making money as the outcome rather than the destination. Our mission is to affect worthy change in our world, to serve our clients (or, in our case, residents and private lenders and investors) and to create new opportunity in the lives of the people on our team. We're on this road less traveled…together.

What kind of important work are you and your company doing? Do you have a fix on it? If not, quantify it. Talk about it. Write it down. Celebrate it, especially as team members contribute to making that unique difference in the lives of your residents and others in your company. And, most of all, model it for others. You set the tone; you embody your mission more than anyone.

FAIR PAY/GENEROUS PAY: People need to feed their families and they have goals beyond the company for which they work. We recognize this. More than anything, fair pay communicates respect; generous pay communicates more respect; getting a "piece of the action" in terms of some kind of ownership communicates I-never-want-you-to-leave type of respect.

The Container Store, named to Fortune List of Best Companies to Work For year after year, lists its First Foundation Principle as "1 Great Person = 3 Good People." Their philosophy is that one great employee delivers three times the business productivity of one good employee.

So, they can afford to pay such employees 50-100% more, spend more hours in training than the competition and, in the process, create a place where other talented people want to work. (For more on them: http://standfor.containerstore.com/our-foundation-principles.)

A person's heart, and with it, his or her willingness to go the extra mile, is given to whom they feel respect from and to whom they respect. When such mutual esteem takes place through a great corporate culture—supportive leadership, high-quality people, even friends to work with, important work to do, generous pay and personal growth as all part of the deal—our team members know they have a real stake in the company and its future.

Their opportunities grow as the business grows, their fortunes rise with the business' profitability and they know, as the company succeeds, so will they, in many more ways than one!

Figure Out Your BIG WHY

Maybe you can articulate your passion, maybe you aren't sure. Either way, the way to energize your passion is to identify your "why." Our why is different than our

Everyone knows WHAT they do. All you need is to review your daily schedule of events. Many of us know HOW we do what we do—our own unique ways that we add a special touch to what we accomplish. But few know WHY they do what they do—and the reason is not to make money (that's a result). Our why is the purpose, cause or belief that gives our organization its reason for existence, its energy and momentum—the very heart and soul of who we are.

Most of the time we go from the right (from the clearest thing) to the left (the fuzzier thing) but the most inspired leaders and organizations think, act and communicate from right to the left

WHY... HOW... WHAT

Allow me to describe how I came to determine my WHY and how that helped me to figure out my HOW and WHAT.

In the summer of 1989, I got Hepatitis A from a local restaurant. As I laid flat on my back staring at the ceiling for two weeks I thought about my future. At the time I was a 35-year old campus pastor at the University of Oregon. I loved campus ministry but it seemed time to make a transition. The question was: What's next?

Maybe you've been in a similar situation, wondering what to do about your future including you financial future.

Nearly a decade earlier I had purchased four properties on the side in Portland but (as some of you remember this) a nasty early '80's recession (a kind of preview to 2008), along with my lack of a coherent business strategy conspired against me. I was fortunate to "get of Dodge," or in my case, Portland, with the shirt on my back.

As I laid in my bed thinking, I knew the potential of real estate, but I hadn't had a good experience with it. However, I also knew sometimes, maybe for often than not, experience teaches you the wrong lesson and I didn't want fear to rule my future choices.

So, the big questions I asked myself: Could I make a go of it now? Could real estate investment be a source of financial stability and even wealth for my family? For me the starting point was simple: feed my family. It was my BIG WHY. (Note: This WHY wasn't to make money, it was to keep my family financially stable so that money wasn't a constant factor that made everything else subservient to finances.)

Over the years that goal (my WHYS) have expanded and even matured as you can note in the sequence below (and you can have more than one). The last two WHYS that are presently energizing my business life and efforts to expand our real estate investment operation.

- **Take care of my Family**
- **Obtain Financial Freedom**
- **Be More Able to do What I'd Like**
- **Build an Enduringly Great Company**
- **Provide Great Opportunities**

What is your BIG WHY? Your WHY is the place to start in thinking about your financial future. Yours may, even likely, be quite different than mine. But the question remains: Why do you want to succeed in this endeavor we're talking about, real estate investment?

Our WHAT and HOW is built on our WHY. It's the core animating principle that drives us and our company, whatever size it is. Your how (plans) and what (action) proceeds from your why (goals). For more

GOALS > PLANS > ACTION

WHY... HOW... WHAT

about WHY>HOW>WHAT see books/articles/videos by Simon Sinek and well as another bestselling book on the subject, *The One Thing*: amazon.com/ONE-Thing-Surprisingly-Extraordinary-Results

Finally, there is the question of implementation, the WHEN. Without the WHEN, the WHY, HOW and WHAT are just ideas and ideas are a dime a dozen without the energy, means and strategy of execution. But you've read this far, so you know this!

KEY QESTION: WHEN?

Tell Your Story

Normally I only get into real estate related business. You did read about my venture into the trucking industry, right—enough said. But I'm compelled to make an exception when it came to Patricia. I meant Patricia in Kansas City when Andrew, Phillip and myself we're just getting started there. She was renting a building next door to our office and I asked her if she knew the name of the contractor's who built the deck on the building.

That's the first time I heard her story. Patricia was a primary care giver to her grandmother, whose name was Margaret, in her final phase of life. Sadly, these were not happy years. After losing her husband her grandmother slipped into dementia and she moved away from her network of friends. The isolation and declining health combined into the grim reality of facing death with very little support systems in place. Her last three years included full-time bed rest and very little human interaction.

In memory of her grandmother, Patricia dedicated her life to the care of seniors. I saw that dedication and the business savvy that I believed would carry it through. So, our company bought the building, took over its rehab. I partnered with Patricia to start *Margaret's Place* which, as you could guess, is named after and dedicated to the memory of her grandmother: facebook.com/MPWellnessCenter

Patricia's mission is to change the way people perceive senior care, first in Kansas City and then beyond. She wants to show a model through her first facility of what she wished was available to her grandmother at that critical time in her life but wasn't. Everyone who meets Patricia hears this story which makes it hard not to want to get involved or at least cheer her on in the fulfillment of her calling.

What's your story? It might not be a dramatic as Patricia but...

Become Mission-Minded

As mentioned in Chapter 11, many years ago Stephen Covey's books (especially *The 7 Habits of Highly Effective People*) replaced my mushy-mindedness with mission-mindedness. What the U.S. Constitution is to our country's founding statement of purpose, our own mission statement is to our personal constitution of life of who we want to be, written, reviewed and altered over time. I created my own 70-word mission statement, which I later boiled down to three indelible words. These key words have guided my life ever since.

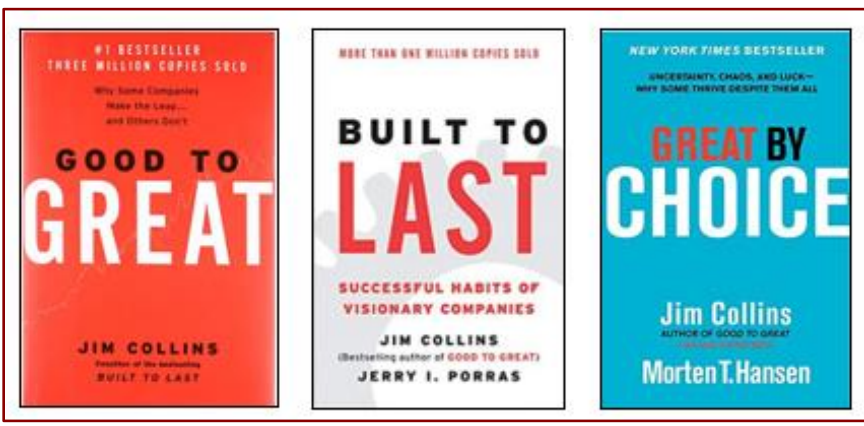
Jim Collins helped me apply similar clarity to my business endeavors. I was so taken by his book *Good To Great* I decided to teach a class on it for real estate colleagues. To prepare, I read his previous book, *Built*

To Last. In this book, Jim Collins and co-author, Jerry Porras, studied such companies which have gained iconic stature, changing the world in their own unique ways like Disney, Boeing, 3M, IBM, Walmart and HP and comparing these companies with others that didn't make the leap to greatness even though they started out with equal or even greater advantages.

I still remember sitting in the sun on a vacation in Mexico with my wife, Teresa, and underlining Collin's various principles used by these companies which helped them to succeed over a very long period. One statement got a double under-line. He said that since you've got to work at doing something in work life, why not work at building…

***An Enduringly Great Company*.**

This book and Collin's three subsequent ones—*Good To Great*, *How the Mighty Fall* and *Great By Choice*—act as the Mount Rushmore of business books, written with 25 years of research from Jim's teams combining 6,000 years of corporate history in their research database.



Collins says that the purpose of these books is to collectively punch holes in the black box that hides the secrets of what it takes to build an enduringly great company. Thanks to Collins the secret's now out. Here's a link to a 30-minute podcast where he summarizes this work: https://www.entreleadership.com/podcasts/jim-collinshow-to-build-an-enduring-gr.

Creating a Business Mission Statement

We have already addressed creating a personal mission statement that acts as your own guiding life-principles. In a similar way, a mission statement should be created to highlight your organizations guiding principles emanating from your hedgehog concept:

What are you deeply passionate about?
What can you be the best in the world at?
What drives your economic engine?

To be effective such statements must be affirmations, regularly reviewed, of a company's special role in the meeting the needs of its customers. They should help the organization re-center itself when forces pull it off course. The statements may be a paragraph or a page long but at some point, they read more like a manual than a mission.

The best mission statements are specific, concise and aptly describe the organization's unique contribution. Here's some one-line summary statements of well-known company's missions:

Disney: *To make people happy.*

Khan Academy: *To provide free world-class education to anyone anywhere.*

Ben & Jerry's: *Making the best possible ice cream in the nicest possible way.*

YMCA: *To put Christian principles into practice through programs that build a healthy spirit, mind and body for all.*

Nike: *To bring inspiration and innovation to every athlete [every person!] in the world.*

Amazon: *To be the world's most customer-centric company.*

The Scooter Store: *To provide freedom and independence to people with limited mobility.*

Facebook: *To give people the power to share and make the world more open and connected.*

Walmart: *To help people save money so they can live better.*

Trader Joe's: *To bring our customers the best food and beverage values and the information to make informed buying decisions.*

Google: *To provide access to the world's information in one click.*

Charles Schwab: *Helping investors help themselves.*

REI: *We inspire, educate and outfit for a lifetime of outdoor adventure and stewardship.*

Wikipedia: *Imagine a world in which every single person is given free access to the sum of all human knowledge.*

In 1989 I choose a name that carried with it the sense of mission I hoped would characterize my then two-person company. What our staff, residents, partners, lenders, vendors, contractors didn't then and don't even now realize, however, is that our name, Stewardship Properties, was meant as a reminder to me: Every day I walk through the office door, see a For Rent sign, sign a document, hand out a business card, I am reminded that I'm just passing through this life: here today, quickly gone tomorrow.

Why the Name?

The name STEWARSHIP comes from the perspective that we are "just passing through this life." While doing so, it is most appropriate to consider ourselves not so much owners of things, but as managers, or better yet, stewards.

It is required of stewards that they be found trustworthy.
-The Apostle Paul, 1 Corinthians 4:2

Stewards are not owners; they are mangers of what has been entrusted to them. Psalm 50:10 says, *The Lord owns cattle on a thousand hills.* I'm pretty sure the implication is that he owns every bit of real estate under their feet as well! I might see my name on a bunch of warranty deeds but I'm not really the owner, just a steward working to be responsible… and here comes our mission statement:

To serve people in their housing needs.

As our business grew, I (we) realized that our customers/tenants (we call them residents) were only served as well as our staff felt a sense of ownership and energized in the process, so we enlarged our mission:

To provide increased and unexpected opportunities for our team
by
serving people in their housing needs.

Finally, as we grew, it dawned on us that there were additional key stakeholders, and our mission statement matured to include them:

Stewardship's Mission

For our residents:
To serve people in their housing needs.

For our private lenders/investors:
To wisely invest their funds, giving them a good return for its use.

For our sellers/vendors/contractors:
To treat them in a respectful, straightforward and ethical way.

For our partners:
To work on their behalf so together we substantially benefit.

For our staff & field team:
To create wealth, enabling increased and unexpected opportunities.

While it's true that some of the world's greatest companies have never officially written down their mission statement, it is also true they have one that guides and rejuvenates their sense of calling. Consider going through the discipline of putting your mission on paper and do so with others on your team, then edit and review it on a regular basis be-cause these statements are not meant to hang as a wall plaques but to provide guidance as living documents.

We never actually arrive; we're always a work in progress. The very act of clarifying, talking about and writing down your mission will help direct your company to fulfill the very mission that is your distinctive and unique work in this world!

Identify Your Brand?
What a mission statement is to our head, a brand is to our heart. To connect with our customers/stakeholders they need to understand the value we bring and tangibly feel its worth, a kind of left-brained/right-brained experience.

Our brand, then, is our heartfelt promise of what we stand for and what others can expect from our products and services. Through their first impressions from our logo, website, hearing our story, or being greeted on the phone, to the "point of sale," to our "return policies," etc., our customers gain an evocative knowledge of our company: who we are, what we stand for, what we deliver. That's our brand.

Branding is the art of aligning what we want people to feel about us as a company with what they feel about us. In that sense our brand is not what we say it is but whatever our customers and stakeholders say it is. No amount of clever, inauthentic branding will ultimately prevail, certainly not in a day of online reviews and social media. It is people who encounter us who will reflect back to us and to the rest of the world what our brand is.

Your brand is what other people say about you when you're not in the room.
-Jeff Bezos

Successful branding requires us to deliver consistent, respectful and positive experiences to earn trust that we (our brand) will do our best at every point of contact: We under promise and over deliver (or not!) and never take them or their experience with us for granted (or not!).

Such alinement helps us to pierce through the incredible amount of noise from the world of marketing to help us gain a competitive edge and get our message across to people otherwise distracted. And, given our genuine efforts to successfully align ourselves with our brand, why not really go for it by working hard to find creative, unique and unusual ways to get the word out that we have great value to add to the lives of our customers.

I don't think this is going to come as a shock, but Stewardship Properties' brand is nothing like Apple's. And likely this is true of your own company. I won't speak for you but I know we are not all that cool or innovative or "different." Neither do we recall the inspiration of Nike or Wikipedia or the delights of Disney or Ben & Jerry's.

There are plenty of things we are not. But what I hope we are is solid, trustworthy and dependable in how we deal with people, their housing needs, their money and their aspirations. When our customers and stakeholders think of the important contribution we make in their lives (our brand) I hope more than anything that an assuring sense of confidence sweeps over them and that they feel (to highjack another company's motto) they're in good hands.

Have you thought about your own brand? What is it? What do you want it to be? When someone tells others about your company, what do/would you want to hear them say? Take a moment with the application worksheet below to think this through. How do you want to build your brand through your marketing materials, online presence, your systems, the personal experiences you and your staff have with those who will reflect back to you what your brand actually is? Maybe you need some professional help with branding. Who can you turn to?

APPLICATION TO YOUR REAL ESTATE INVESTMENT BUSINESS

CHAPTER 13: Mission-mindedness sets priorities

If you have a leadership team, we'd suggest getting them together for this exercise over a period of time. The process of creating, reviewing and updating a mission statement is just as important as statement itself in making it become a living reality within your organization.

Define your company's mission statement. Put it in rough draft below, then write it again on another piece of paper. Later involve your team and refine the statement together:

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Describe your brand. How do you want to be seen by your customers and stakeholders?

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What needs to change in your company to be more compatible with your brand?

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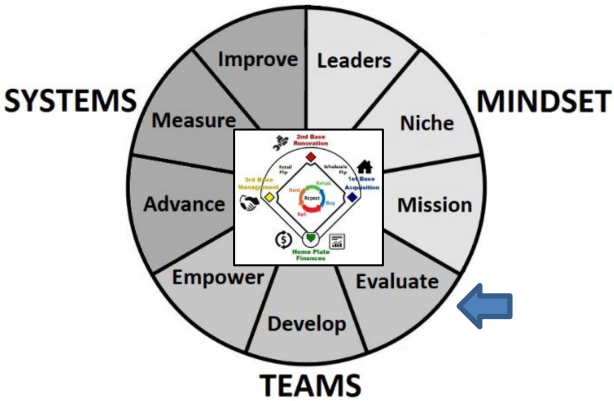


PART 3

HIGHLY PRODUCTIVE TEAMS

CHAPTER 14 / Step 4

TEAMS: Evaluate the right roles for the right people

My (Bill) very first employee nearly 30 years ago was a woman named Anne. I knew Anne from church. She was pleasant, kind and friendly. She was also incompetent. Granted, she might have been great at any number of jobs, but I wanted her to do bookkeeping and oversee some property management. Little did I know how little she knew.

None of this was her fault. I never interviewed Anne nor had a job description nor even a viable set of expectations. So, who was I to say she was incompetent for what I hired her to do!? That was left to an auditor from the Real Estate Agency.

At the time our company did some property management for other owners and we had gotten a complaint which led to the auditor showing up at our door. As it turned out we were the ones owed money, not the reverse, but Anne who labored for months trying to redo faulty bookkeeping, would never have been able to figure that out.

Fortunately, along came Stacie. Stacie was a young friend who I knew was great at math, had an incredible memory and was wicked smart. In my mind at the time, that was good enough to be a bookkeeper. Fortunately, Stacie was able to go through every check, every receipt, every everything and as the patience of the auditor began to run thin, presented him with the kind of accounting he insisted on.

As you might imagine Stacie became an anchor employee in my growing business. I more than teared up the day she left a decade later for a job with the county. I knew her presence testified to my good fortune, certainly not to my hiring savvy.

On the list of important things, hiring is the most important thing a business leader does. The quality of your business, prospects for grow and ability to seize new opportunities rises or falls on the strength of your team. Of course, you team will include people who aren't your employees like partners, specialists, contractors and other experts in your network. But those who work directly for you—your team members—will make the critical difference on a day-by-day basis.

For the sake of simplicity, when it comes to hiring and firing people one can divide employees into three categories: A, B & C players.

C players may be enthusiastic, but they tend to see the company's mission revolve around themselves rather than the larger picture. So, they quickly devolve into small ambitions and petty issues. Because they view the company revolving around them, they will often do the minimum. When mistakes happen, they blame shift. They let problems fester: "It's not part of my job."

They are not team players in the sense that they pitch in, doing whatever it takes to make something happen. They think in strict categories and job descriptions: "This is not my responsibility, it's someone else's." They want to get promoted for the purpose of making more money, but not to test themselves in taking on more responsibility and excelling at the next level.

The second part of the adage, “hire slow, fire fast” is very appropriate with C players. Our first inclination that “things aren’t working out” should be *the signal* that “things will never work out.” We shouldn’t see having to fire someone as a failure on our part because it is not easy to get it right, and we’ll likely get it wrong as often as we get it right.

The only thing to consider a failure on our part is to keep someone on that we know we need to fire. At that point, every day they are with us is a day our business is either going backward or, at best standing in place. It’s not good for them, and certainly not good for the morale of others who are looking for that person to pull their weight. Our credibility is on the line as to what kind of quality we expect out of our people.

In *Good to Great*, Jim Collins has a helpful illustration about a bus (company). Companies that excel know that some people who are on the bus need to change seats (which is admittedly difficult in small businesses) while others need to get off the bus entirely and these are C players.

That being said, egos are fragile things and we should be careful when we fire people. If they really want honest feedback, it could be a good thing for them. But it might be wise to “blame ourselves” when we tell them why we are letting them go. Bottom-line is that we should approach firing carefully for the sake of our company (others in our company want to know we treat people, even those we terminate, with respect) and for the sake of the person we are letting go. (Likely there is another bus that will come along that is a better place for them.)

B players fall into two categories: Those who will always be B’s—the B- players (the majority)—and those who have the potential to become A players, the B+ players. Their grade has nothing to do with their initial grasp of the job—they may not know their way around this job’s specifics or even have had any real experience in the position. They do need “basic smarts.” But it’s mostly about their ability to adapt and their mentality to learn, grow and excel. Their work environment plays an important role. So, while an “A outcome” is possible, in the wrong environment, a “C outcome” is just as possible.

B- players are what you might call *cul-de-sac people*. They can do what they were hired to do, but not much more. They are proficient and even efficient at getting things done but they are not going to stretch and really improve themselves. They may have their “job down” but they are not going to work hard at coming up with new ideas to improve the business. They may be competent, but they are also content…and this is the problem. They often ask for approval (“what should I do next”) and seldom act as a “self-starter.” Even if they “buy into the company’s mission” they cannot help fulfill it because they are focused on their own small sphere of influence and not much else.

My recommendation is that when we realize someone is B- player he/she should be let go. Our temptation is to keep them on, hoping they’ll improve, but we usually know this will not be the case and we need to make the hard decision to move on quickly.

Now, I must say there are plenty of “B Businesses” out there. B people (both B-, B and B+ players) populate these companies. People are making a living but there isn’t much commitment to real growth. Bob Dylan’s lyrics fit here: “Those who aren’t busy being born, are busy dying.” In other words, most companies can’t just keep the status quo. They are either moving ahead to fulfill their mission or they are going backward.

Of course, the economy can affect some businesses quite dramatically, testing them to the very limits of their capacity to adapt to changing environments. Companies that survive such downturns are to be most admired. They also must have A players in their ranks!

B+ players have the potential to become A players but it will be quite challenging for them. They need an “internal energy,” a spark that can become a flame and then a fire of desire to better themselves. And to become an A player they will need something more: Intense training and an empowering environment. The clue between B- and B+ players is that B+ players are *capacity people* (rather than *cul-de-sac people*). They can stretch and grow with the job and make themselves and the company better. (B players are somewhere in the middle.) B+ players look for new challenges and take them on.

They are genuine contributors. BUT, and this is important, they can fall backward into "minus status" if they are not mentored carefully and consistently. B+ players are a challenge to business owners because they take time to teach and train. If it is not our goal to see them become A players, they likely won't. And if our company is not looking to really excel it will also take away any potential for a B+ player to become an A player.

A players are the only ones we really want to hire. Okay, it's true that businesses can grow with B and B+ players but they will also be hamstrung in their growth by the fact that the owner's smarts, capacity and span of control will be about the extent of the company's ability to grow.

A players are definitely "capacity people" and self starters. They're okay with making mistakes. They want to master something and then learn the next thing and then the next. They constantly think about ways to improve themselves and the company and they aren't afraid to share those ideas with the powers that be.

Consequently, A players can be intimidating. They will always have ambitions of their own and our company may be seen by them as a steppingstone to something better. We are the opportunity for today but maybe not for tomorrow. A players could very well learn enough to become our competition and then leave. That's just how it is.

This fact is embraced as a challenge to "A Business Owners." Such owners do not see A players as a potential threat so much as a potential partner and, if being a partner is not good enough for the A player, so be it. “A Business Owners” are going to hire them anyway and after they leave, work at forming a strategic alliance with them.

A players require business owners to have an *abundance mentality* rather than a *scarcity mentality* of being threatened by their abilities and ambitions. They also challenge owners because A players want to work for companies that are really going somewhere, to the next level and beyond. If they see a future for themselves in this company they “buy in” in a big way and help the company reach the next level and the level after that. A players want more income, who doesn’t, but they crave making their mark and see money as a barometer that they are having a more positive influence in the company.

We should always be on the lookout for A players and see if there is anyway to fit them into our company even if it means an initial financial strain. That being said, A players are not that easy to find and…this is why we should always be looking for them! At the minimum we should look to associate with A players because they have an abundance mentality and will challenge us to go beyond where we are right now.

Hiring & Firing. Don’t underestimate the significance of a person’s job experiences when interviewing them for the position:
How well did they do? This could take hours. (We’ll want to talk to former boss/owner.)

Did they leave with a positive feeling among their co-workers and especially their boss?

What contributions did they make? This should be very specific for every work position.

Again, figure on making this a long conversation. How do they feel proud of their accomplishments? How did each accomplishment make a real difference to the business?

(Think of the kind of person you want to work for you: Is this that kind of person? Can you envision this person one day being a partner, even if it's a small percentage?)

A big red flag is if they left with bitterness or if they have bad things to say about their former employer or their job situation. Were they a "victim of their circumstances" (this has C or B- player written all over it) or did they do whatever it took to positively improve those circumstance and make them better (like a B+ or A player)?

We will not change people very much. This is the bottom-line. Some can change with a very positive work environment and with solid mentoring (B+ players). They just have not yet been given a chance to bloom. BUT most people, by the time they are in their 20's are who they are, and this is even truer of 30, 40 and 50-year olds. Their choices and their previous environments have made them into who they are and we are going to do precious little to change them.

So, only look to hire A players. And when you do: hire slow, fire fast. Be okay with making a mistake. The only real mistake is to not let someone go when you need to in order to refocus on hiring that genuine A player.

Then after hiring the right person, it's time to focus on the business-accelerating work of coaching them up to reach their full potential…all the while evaluating if this is the right person for this particular job!

NOTES

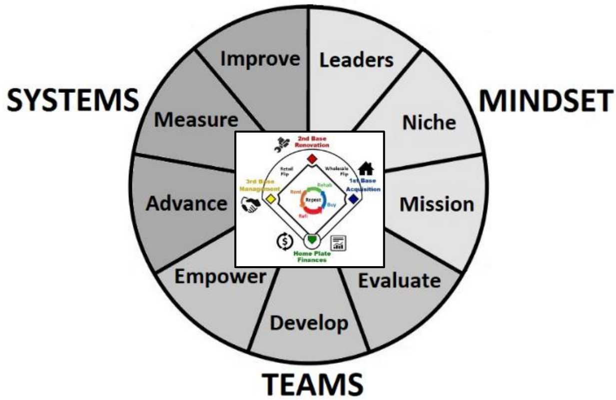
How would you describe the culture of your company?

Do you have the people you want? How would your rate them (A/B/C)? Any you need to help move seats or off the bus?

What are you doing to find more A players?

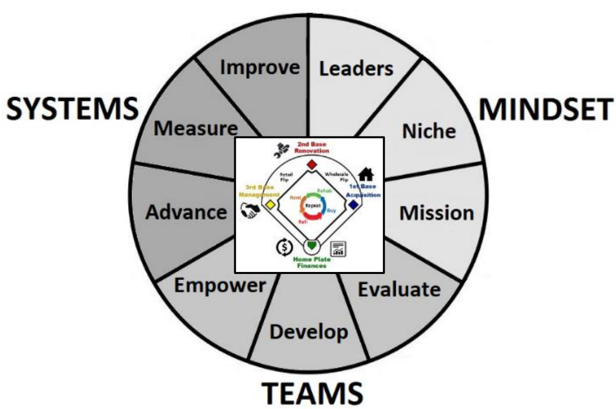
What are you doing to mentor those you have?

The following chapters are notes and comprise an uncompleted remainder of this book.



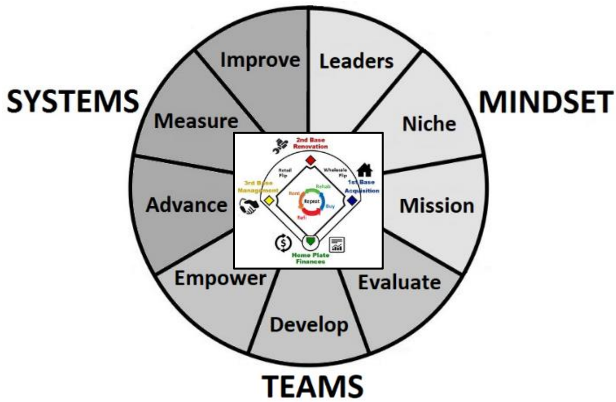
CHAPTER 15 / Step 5

TEAMS: Delegate everything someone else can do



CHAPTER 16 / Step 6

TEAMS: Motivate through a results-oriented culture

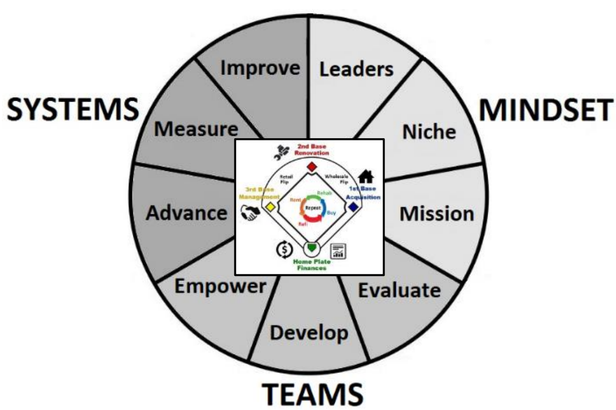


PART 4

EXECUTION OF SYSTEMS

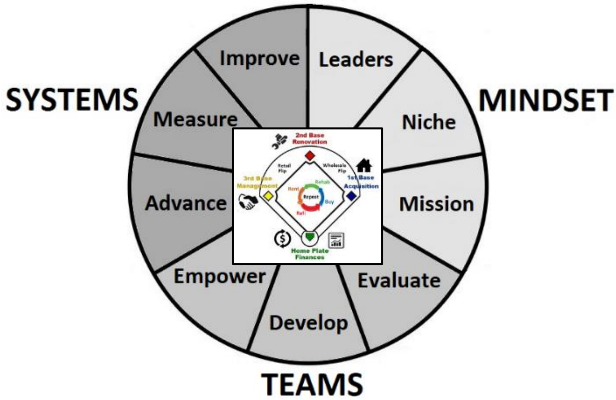
CHAPTER 17 / Step 7

SYSTEMS: Advance Strategically



CHAPTER 18 / Step 8

SYSTEMS: Measure Consistently

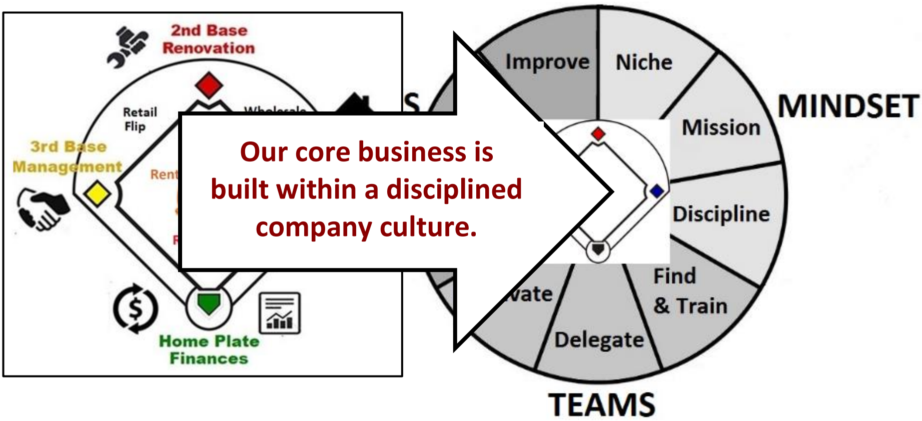


CHAPTER 19 / Step 9
SYSTEMS: Improve Continually

YOUR FUTURE
The GROWTH of Wealth Creation

CHAPTER 20
What Got You Here Won't Get You There

Stewardship Properties' Investment Strategy



Stewardship Properties' Mission

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